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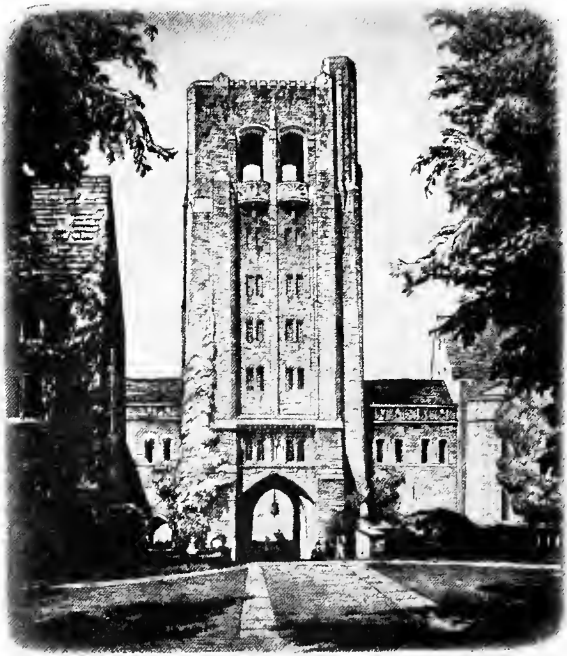

# THE LAW OF PARTNERSHIP.

*By the Same Author.*

The Law of Sales of Personal Property.

Cases on the Law of Sales.

Cases on the Law of Partnership.

THE

# LAW OF PARTNERSHIP,

INCLUDING

# LIMITED PARTNERSHIPS.

BY

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# PREFACE.

THIS book is the result of an attempt to state clearly and concisely the principles of English Partnership Law, with an especial view to the needs of the student, as these have revealed themselves to the writer during his repeated discussions of the subject in the lecture-room. It is a branch of the law which has never proved to be particularly simple or easy for students, and the writer is fully conscious that he has not wrought any radical change in its nature. He has tried to point out the chief sources of difficulty, however, and to save the student from needless perplexity. While he has not hesitated to criticise respectfully judicial decisions, which appear to him unsound and confusing, nor to avow his own opinions upon controverted points, he has striven not to theorize unduly, but has sought to state the law as it is.

In dealing with the topic of Bankruptcy, it became necessary to examine with care those provisions of the United States Bankruptcy Law of 1898 which relate to partnership, and to consider the extent to which

they have modified former rules. It is believed that some of the changes which they have produced are not only important but are even radical.

Legislation has added a chapter to Partnership Law in this country, by its institution of Limited Partnership. In treating this subject, however, no attempt has been made to enumerate the various statutes nor to point out their differences in detail. Discussion has been confined to the principles which are applied in organizing and administering this form of partnership. In order that the reader may have easy access to a typical statute on this topic, the New York Partnership Law of 1897 has been reprinted as an Appendix.

Columbia University School of Law,
February, 1899.

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# THE LAW OF PARTNERSHIP.

## INTRODUCTION.

### § 1. A Modern Branch of English Law.

MOST of the rules relating to partnership in English law have been developed within a little more than a century. No discussion of them is found in Blackstone's Commentaries, and even his allusions to the subject are few and casual.[1] In the early abridgments and digests, the few reported cases on this topic are widely scattered under various heads, such as Accounts, Merchant, Survivorship. Even Viner, who appears to have been the first to collect them under the title of Partnership, found no difficulty in compressing them into less than six pages of the ten thousand and more which make up his twenty volumes.[2]

Undoubtedly the Italian bankers, who carried on their trade by means of large "societies" or companies, began to teach Englishmen "a little about partnership,"[3] during the reign of Edward I.; but Englishmen do not seem to have put that knowledge to much practical use until the closing years of Elizabeth's reign, when the rapid expansion of commerce opened their minds to the advantages to be gained by uniting the capital and skill of several individuals in a common enterprise.

[1] 2 Bl. Comm. 399 (no survivorship among partners). 3 Ibid. 437 (courts of equity have jurisdiction of partnership accounting).

[2] Vol. 15 (1742).

[3] 2 Pollock and Maitland's Hist. of Eng. Law, 219.

(*a*) *Paucity of Decisions in Early Reports.* — For a century or more after partnership became an established and successful institution of English commerce, it rarely occupied the attention of English courts of justice. Probably this is due to the fact that, during a part of this period, disputes between merchants were disposed of by Merchants' Courts. Even when these died out, and the disputes came before the law courts for determination, the judges, prior to Lord Mansfield's time, had the habit of leaving to the jury not only the facts of each case, but the custom of merchants applicable thereto, "with a result that cases were rarely reported as laying down any particular rule, because it was almost impossible to separate the custom from the facts."[1]

It is not surprising, therefore, that the first attempt to bring the law of partnership into a systematic form was not made until the closing years of the eighteenth century; nor that the treatise[2] then published possesses but little value for the student or practitioner of to-day.

### § 2. Incongruous Elements in English Partnership Law.

A learned writer has said: "The law of partnership rests on ~~a foundation composed of three materials; the Common Law, the law of Merchants, and the Roman law."[3] It must be added that these different materials, like the iron and the clay in the image~~ of Nebuchadnezzar's vision, do "not cleave one to another." Nor has English jurisprudence yet shown its ability to assimilate them.

This diversity of materials in the very foundation of English partnership law will constantly force itself upon our attention as we proceed with our subject. We shall discover, from time to time, not only a lack of affinity

1 Scrutton's Mercantile Law, 13 (London, 1891).

2 Watson on Partnership (London, 1794).

3 Collyer on Partnership, 1.

but positive repulsion between common law principles and the usages of merchants. A single example will suffice by way of illustration.

The law of merchants recognized a partnership as an entity separate and distinct from the members composing it; such is still the mercantile conception of a firm. This quasi person holds the title to the firm property. It acquires rights and incurs obligations of its own. It may deal even with its own members, thus becoming their creditor or debtor. But the common law flouts all such notions. It refuses to personify the firm. A partnership is but an association of individuals. It cannot contract with its members, because a man cannot contract with himself. To this conflict of views is due much of the confusion and perplexity which characterize some of the branches of our partnership law.

(*a*) *Futile Attempts at Assimilation.* — Neither in England nor in this country have these views been harmonized; nor have the legal rules relating to partnership been reduced to a thoroughly coherent system, although repeated attempts at unification have been made. For example, the experiment has been tried of bringing the legal rules into conformity with the mercantile conception of a partnership;[1] but the doctrine of *stare decisis* has deterred the courts from joining effectually in this movement, and legislation has given it but a fitful and uncertain support. One of the severest critics of this experiment has attempted to systematize the law of partnership upon the basis of firm property. "The instant the notion of firm property is brought forward," he declares, "the material is furnished for an explanation of the relation in all its bearings."[2] But this attempt has been received with even less favor than its predecessor; and the pro-

[1] See Parsons on Part. (4th ed.), §§ 1, 3, 4, 46.

[2] Parsons (Jas.), Principles of Part. (1st ed.), lxv.

fession is still "groping about in search of . . . some single guiding and controlling principle, . . . on the basis" of which the law of partnership may have "an orderly development."[1]

Not so in England, where the quest of any such principle has been abandoned, and the law of partnership with its existing incongruities has been codified.[2]

[1] Parsons (Jas.), Principles of Part. (1st ed.), lxv, and 37 Am. L. Reg. N. S. 141. What Constitutes a Partnership, by Geo. Wharton Pepper.

[2] British Partnership Act, 1890. See Pollock's Digest of Part. (3d ed.), xxi, and Pollock's Essays on Jurisprudence, 95, for an optimistic view of the present state of partnership law.

# CHAPTER I.

## THE FORMATION OF A PARTNERSHIP.

### § 1. Partnership results from Contract.

THE relationship of partners is not imposed by the law upon individuals, but is created by their voluntary assent. In the language of an early writer: "Societie is a contract by consent about a thing to be had or used in common on both sides. . . . But that only is properly called Societie, which by mutuall consent is applied to that end, that there may be partnership or fellowship among the persons contracting; wherein so soon as they are fully agreed, the one is properly called the others fellow." [1] This doctrine, originating in the Roman law, became a part of the law merchant, and has been uniformly adhered to by common law courts in litigations between partners themselves; although, as we shall see hereafter, it was discarded for a time in England, and is still questioned in some of our jurisdictions, when the rights of third persons are involved.

(a) *An Early Decision of the House of Lords.* — It is true that the Court of Chancery once decided that a partnership existed which "did not arise by contract," but the decree was reversed by the House of Lords. In that case, a London trader invited his nephew to remove from Hamburg, with a view to becoming a partner. Upon the nephew's removal, a new set of books was opened, in which he appeared as a partner, and his name was used as that of a member of the firm for about two years. No

[1] West's Symboleography (1590), § 26.

articles of partnership were entered into, however, and the uncle, when giving the invitation, had expressly notified the nephew that he was "to expect no benefit from the trade," unless he succeeded in marrying a woman with a fortune of twenty thousand rix-dollars. In the course of about two years, the uncle found that the nephew "had not that turn to business which was likely to prove advantageous to either of them," and as the nephew had not succeeded "in such a match" as had been stipulated for, the uncle sent the nephew home, and formed a partnership with another person. No accounting was had between them, nor was any claim made by the nephew against the uncle during their lives. After their deaths, the representatives of the nephew filed a bill for a moiety of the stock and of the profits of the trade for the two years during which the nephew's name had been associated with his uncle's in the business. The Court of Chancery having "declared that the testator and his nephew ought to be looked upon as partners, and that such partnership did not arise by contract," the decree in favor of the complainants was reversed by the House of Lords, and upon a trial at law in the King's Bench "a verdict was found that the partnership was nominal only, and not real."[1]

(*b*) *Other Examples.* — A broker buying goods for several undisclosed principals, who are to have separate shares therein, is not brought thereby into partnership relations with them. The transaction is not one in which the parties "meet and contract together as partners."[2] Nor does the master of a ship become a partner with a friend who furnishes money, with which the master buys goods to be taken by him on a voyage, although it is agreed if any profit shall arise from them the friend shall have one half for his trouble. It is only "an agreement

[1] Jacobsen *v.* Hennekenius, 5 Bro. P. C. 482 (1714).

[2] Hoare *v.* Dawes, 1 Doug. 371 (1780) ; Burdick's Cases on Part. 1.

for so much, as a compensation for the friend's trouble, and for lending the master his credit."[1] Even the joint owners of a cargo, bought with the proceeds of an outward cargo, are not partners unless they have contracted with each other for that relationship.[2]

Again, a trader cannot convert his creditor into a partner by agreeing to pay the latter a share of the net profits of the business, in addition to interest;[3] and the creditor of a partner, by taking an assignment of his debtor's share in the firm, and arranging with the other partner for closing out the business, does not become a partner in such business. A contract for "a community of interest by way of security for the payment of money" is radically different from "one of partnership."[4] The idea of "surprising parties into a partnership"[5] is not favored by the courts.

1. Why an Actual Contract is required. — The reason for this requirement is found in the nature and the consequences of a partnership. Property, contributed to a firm by its members, is no longer owned by them in severalty, but the ownership is vested in the firm. One tenant in common of a chattel can dispose of his share, but cannot alienate the share of his cotenant. A partner, on the other hand, can transfer a perfect title to firm chattels. Again, one tenant in common cannot bind his cotenant by a contract relating to the common property, without special authority. The contract of any partner, within the scope of partnership business, binds not only the firm property, but each member of the firm.[6] "When a

[1] Hesketh v. Blanchard, 4 East, 144 (1803).

[2] Holmes v. United Ins. Co., 2 John. Cas. 324 (1801).

[3] Ex parte Briggs, 3 Dea. & Ch. 367 (1833); Burdick's Cases on Part. 3.
3
3

[4] Fish v. Thompson, 68 Vt. 273; 35 At. 174 (1895).

[5] Phillips v. Phillips, 49 Ill. 437 (1863).

[6] Hopkins v. Forsyth, 14 Pa. St. 34 (1850).

man enters into a partnership," said Lord Kenyon,[1] "he certainly commits his dearest rights to the discretion of every one who forms a part of that partnership in which he engages." "It is an imprudent thing for a man to enter into partnership with any person, unless he has the most implicit confidence in his integrity. . . . One partner may pledge the credit of the other to any amount."

(*a*) *Importance of Delectus Personarum.*—Freedom of choice as to his associates, therefore, is a matter of the highest consequence to one entering into a partnership. His right to exercise such a choice is a fundamental principle of partnership law.[2] Hence the rule that "No person may be introduced as a partner without the consent of all existing partners."[3] Even the personal representative of a deceased partner is not allowed to take the place of his testator in a firm without the consent of the surviving partners. "It would be of ill consequence in general to say, that in articles of partnership in trade, when no provision for the death of either partner is made, they might subsist for the benefit of an executor who may not have skill therein."[4]

Undoubtedly partners may bind themselves to receive in his stead the personal representative of a deceased member,[5] although they cannot force such representative

[1] Wells *v.* Masterman, 2 Esp. 731 (1799); Baker *v.* Charlton, Peake, 80 (1791).

[2] Lindley on Part. 363 (5th Eng. ed.).

[3] Partnership Act, 53 & 54 Vict. c. 39, § 24 (7).

[4] Pearce *v.* Chamberlain, 2 Ves. Sr. 33 (1751).

[5] Warner *v.* Cunningham, 3 Dow, 76 (House of Lords, 1815). Neighbors in Ayrshire formed a partnership for 124 years in working their adjoining coal fields, binding their heirs and assigns to the performance of the contract. After the death of Warner, his heir sought to renounce the partnership, but the Court of Session held that, while the heir might throw up the succession, if he thought the partnership too hazardous, yet if he accepted the succession he must abide by the

to become their partner.[1] He also possesses the right to select his copartners. If, however, he decides to avail himself of such a stipulation in the partnership articles, and to enter the firm in his testator's stead, "he places himself in that situation by his own choice, judging for himself whether it is fit and safe to enter into that situation and contract that sort of liability." [2]

2. CONTRACT MUST BE ENFORCEABLE. — (*a*) *A Consideration is Essential.* — It is necessary, not only that the parties voluntarily assent to become partners, but that their agreement be such as to impose legal obligations upon them. If the arrangement is that one shall furnish all of the capital and services, while they shall share equally in the property acquired and the profits gained, no partnership ensues. "It is a naked promise founded upon no consideration." [3] But if the parties "mutually agree to form a partnership for the purpose of making a proposed road improvement, in case the contract for making the same should be awarded to either of them, and that the contract so awarded should inure to the benefit of the copartner-

partnership. On appeal to the House of Lords, the appellant's counsel argued that, as the Roman law was followed in Scotland, its rules declaring void a stipulation for admitting the heir of the deceased into the firm, and securing to each partner the right to renounce the partnership at any time, should be applied in this case. Respondent's counsel replied that "the Romans were not a commercial people, and therefore a question of partnership was not to be judged of by the civil law, but by the laws and customs of modern Europe." The decision of the Court of Session was affirmed in every respect. *Cf.* with the foregoing quotation, this remark of Chancellor Kent: "In the Roman law, and in the commentaries of the civilians, every subject connected with the doctrine of partnership is considered with admirable sagacity and precision." 3 Comm. 56.

[1] Wild *v.* Davenport, 48 N. J. L. 129; 7 At. 295 (1886); Burdick's Cases on Part. 77.

[2] Ex parte Garland, 10 Ves. 109, 119 (1804).

[3] Mitchell *v.* O'Neall, 4 Nev. 504 (1869).

ship, . . . the undertaking of each party is based on the undertaking of the other, which, in law, is a sufficient consideration to support the contract."[1]

(*b*) *Contractual Incapacity.* — An agreement to establish a partnership may fail of its purpose, because of the incapacity of the parties to enter into a contract. Lord Justice Lindley has said:[2] "Now that the disabilities under which spiritual persons formerly lay have been removed, the writer is not aware that there is any class of persons (except convicts), who, being of sound mind, and over twenty-one, are rendered incapable of becoming members of a partnership. Married women may be partners, as will appear later on." This statement is open to criticism. Not only are convicts incapable of entering into a partnership,[3] but alien enemies[4] and corporations[5] (in the absence of charter authority) are subject to a like incapacity.

In England, the common law disabilities of married women have been so far removed that their partnership agreements are entirely valid and binding. The same re-

[1] Breslin *v.* Brown, 24 Ohio St. 565 (1874); Coleman *v.* Eyre, 45 N. Y. 38 (1871); Belcher *v.* Conner, 1 S. Car. (1868), *accord.* In the last case it was said: "The contract sought to be enforced is one of partnership. The business contemplated by it was the purchase and sale of slaves; but the proper consideration of the contract was the mutual covenants and promises of the copartners, and the acts they respectively engaged to perform, bearing on the objects contemplated. It cannot, in any just sense, be said that a contract of this nature was one of which the consideration was the purchase of slaves."

[2] Lindley on Part. (5th Eng. ed.), 71.

[3] A matter of statutory regulation. See N. Y. Pen. Code, §§ 707, 708, and N. Y. Code of Crim. Proc., § 819; Avery *v.* Everett, 110 N. Y. 317 (1888).

[4] Griswold *v.* Waddington, 15 Johns. 57 (1818); Burdick's Cases on Part. 544.

[5] Gunn *v.* Railroad, 74 Ga. 509 (1885).

sult has been reached in some of our States;[1] while in others, legislation, as interpreted by the courts, has not accomplished the wife's business emancipation. For example, in Massachusetts, a married woman may be a member of a trading partnership, if her husband is not a member thereof;[2] but if he is a member, her agreement to enter the firm is null and void.[3] "If she could contract with her husband," said the court in the case last cited, "it would seem to follow that she could sue him and be sued by him. How such suits could be conducted, with the incidents in respect to discovery, the right of parties to testify, and to call the opposite party as a witness, without interfering with the rule as to private communications between husband and wife, it is not easy to perceive; and the consequences which would follow in respect to process for the enforcement of rights fixed by judgment, arrest, imprisonment, charges of fraud, proceedings *in invitum* under the insolvent laws, and the like, are not of a character to be readily reconciled with the marital relation. We cannot suppose that an alteration in the law involving such momentous results, and a change so radical, could have been contemplated by the legislature, without a much more direct and clear manifestation of its will."

3. Statute of Frauds. — Two provisions of this statute bear upon our present topic. One of them requires that any agreement that is not to be performed within the space of one year from the making thereof shall be in writing. Accordingly, if the partnership contracted for is not to commence within a year from the making of

[1] Swan *v.* Coffe, 122 N. Y. 308; 25 N. E. 488; Burney *v.* Savannah Grocery Co., 98 Ga. 711; 25 S. E. 915 (1896); Burdick's Cases on Part. 11.

[2] Plumer *v.* Lord, 5 Allen (87 Mass.) 460 (1862).

[3] Lord *v.* Parker, 3 Allen (85 Mass.) 127 (1861).

the contract, or is to continue for more than a year thereafter, the agreement must be in writing or it will not be enforceable. Nor will such a contract be taken out of the statute by part performance. Undoubtedly a partnership business may be lawfully carried on under such a contract, but the partnership can take effect only as a partnership at will.[1]

The other provision requires that any contract for the sale of lands, or any interest therein, shall be in writing. Does this render an oral contract for a partnership in lands unenforceable? It must be confessed that the authorities are far from harmonious on this point. Some declare that the partnership is validly organized under such a contract, and that the rights of the partners in the lands of such a firm may be established by oral evidence.[2] Others insist that, while a valid partnership may be created by oral agreement for the purpose of dealing in lands, and the rights of the partners in lands bought with partnership funds may be shown by parol, wherever the transactions give rise to a resulting trust in favor of the partners, yet if the agreement provides for a partnership in lands which are at the time owned by one[3] or both[4] of the parties, or thereafter to be acquired by one of them,[5] it is within the ban of statute. The latter view is supported by the great weight of authority in England as well as in this country, and is preferable upon principle. The property which each partner agrees to contribute to the firm is not vested in the firm by the legal force of

1 Wahl *v.* Barnum, 116 N. Y. 87; 22 N. E. 280 (1889).

2 Dall *v.* Hamilton, 5 Ha. 369 (1846). "This is certainly going a long way towards repealing the statute of frauds." Lindley on Part. (5th ed.) 82.

3 McCormick's Appeal, 57 Pa. St. 54 (1868).

4 Goldstein *v.* Nathan, 158 Ill. 641; 42 N. E. 72 (1895); Burdick's Cases on Part. 9.

5 Smith *v.* Burnham, 3 Sumn. 435 (1838).

the partnership contract. His individual ownership is devested only by some act over and above the act of contracting; and that act, whenever it is done or in whatever it consists, if the contribution to be made is of real property, amounts to a transfer from him to the firm or to his copartners of an interest in lands.

4. Express Contract Unnecessary. — While the relation of partnership arises only from contract between the parties to that relation, and while the terms of their agreement are ordinarily set forth in written articles, neither a writing nor any particular form of convention is essential. A valid partnership may subsist, although no express engagements of its members can be discovered. Its existence may be established by the conduct of the parties.

In a recent case,[1] the question whether a partnership had existed between the plaintiff and a deceased brother was submitted to the court upon an agreed statement of facts, which included the following: "No articles of partnership were ever executed, nor any agreement for a partnership come to, nor was a partnership ever mentioned between them. No accounts as between them were ever kept, nor was any balance-sheet or annual account as to the business prepared." And yet, as these brothers had acted together in carrying on a business bequeathed to them by their father, had drawn out and retained each week precisely the same sum, had carried on the business in such a way as to make them liable as partners to outsiders, and had borrowed money for the business on their joint mortgage, the court reached the conclusion that the two brothers were partners by agreement.

(*a*) *Words are not Conclusive.* — On the other hand, the relationship between persons having a common interest in certain property, or in a particular enterprise, is

[1] Davis *v.* Davis, [1894] 1 Ch. 393; Burdick's Cases on Part. 12; Rutger *v.* Rutger, 28 N. J. Eq. 137 (1877).

not that of partnership, although they may call it by that name. When the entire agreement as well as the conduct of the parties is considered, it may be evident that the term was used in a popular and not in a legal sense,[1] or it may appear that they have failed to accomplish their purpose. "Where the question of a partnership is to be determined from a contract between the parties to it, the relation must be found from the terms and provisions of the contract, and even though parties intend to become partners, yet if they so frame the terms and provisions of their contract as to leave them without any community of interest in the business or profits, they are not partners either in fact or law."[2]

When there is no conflict of evidence in a case, whether a partnership "existed or not is an inference of law from the facts," and though the testimony of a party that he and certain others were partners is uncontradicted, it may "have no effect."[3]

16. [1] Oliver v. Gray, 4 Ark. 425 (1842); Burdick's Cases on Part. 16; Livingston v. Lynch, 4 John. Ch. 573, 592, 593. The owners of a steamboat company styled themselves "sole proprietors and acting partners," and yet were declared by the court to be only tenants in common. This popular use of the term partners is often misleading. In 11 Polit. Sc. Quarterly, 265, note 2, it is said: "The Turkey or Levant merchants were first chartered as a partnership (1581), and in 1592 were incorporated. Hakluyt, Collections, vol. ii. pp. 263, 434." The charter of 1581 does style the grantees in the letters patent "parteners, adventurers, or doers," but it bestows corporate powers upon them, provides for the introduction of new members without the consent of all; for the election of a "Governor of the said company," and for his removal; for the granting of licenses to trade by the governor and company, and for the adoption of reasonable laws and ordinances for the good government of the company. The association had none of the legal characteristics of a partnership. It was in fact and in law a corporation.

[2] Sailors v. Nixon-Jones Co., 20 Ill. App. 508 (1886).

[3] Dwinel v. Stone, 30 Me. 384 (1849). Burdick's Cases on Part. 17.

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### § 2. Specific Intent to form a Partnership is not Essential.

Although the partnership relation cannot be instituted without the assent of the parties thereto, it does not follow that the specific intent to incur the liabilities of partners is necessary to the existence of a partnership.[1] "It is possible for parties to intend no partnership and yet to form one. If they agree upon an arrangement which is a partnership in fact, it is of no importance that they call it something else, or that they even expressly declare that they are not to be partners.[2] The law must declare what is the legal import of their agreements, and names go for nothing when the substance of the arrangement shows them to be inapplicable."[3]

Persons associating themselves as stockholders in a grocery store business, and thus voluntarily becoming the owners of such business, are partners, even though they do not intend to form a partnership. "Their belief, or understanding, that during that time they were not partners, in the legal sense of the word, was a mistaken and immaterial view of the law." "The supposed limitation of their liability was mere legal error."[4]

### § 3. A Common Business with a View of Profit.

We have seen that the existence or non-existence of a partnership does not depend altogether upon the language of the contracting parties, nor upon the specific intent

20 [1] Green *v.* Beesley, 2 Bing. N. C. 108 (1835); Burdick's Cases on Part. 20.

[2] See Scott *v.* Campbell, 30 Ala. 728 (1857), where an arrangement made between partners upon the dissolution of their partnership, and which was plainly intended by them to prevent the continuance of their partnership relations, was held to constitute a partnership *inter se.* *Cf.* Duryea *v.* Whitcomb, 31 Vt. 393, 395 (1858).

[3] Beecher *v.* Bush, 45 Mich. 188 (1881).

[4] Farnum *v.* Patch, 60 N. H. 294 (1880).

which actuates them when entering into an association. They may give to their relationship one name, but the law may give to it quite another name. Whether their misnomer proceeded from a misapprehension of the law, or from a desire to evade partnership liabilities while sharing its benefits, it is equally ineffective with the courts. How, then, does the law determine whether or not a partnership exists between particular associates?

1. Statutory Rules in Britain. — This question has received an authoritative answer in Great Britain by an Act of Parliament. "Partnership," in the words of that statute, "is the relation which subsists between persons carrying on a business in common with a view of profit."[1] After announcing this general principle, the statute lays down several rules to be followed in applying it.[2] The

[1] Partnership Act (53 & 54 Vict. c. 39), § 1 (1). The second subsection excepts from this definition registered joint stock companies, corporations, and mining companies under the jurisdiction of the Stannaries.

[2] Ibid., § 2. "In determining whether a partnership does or does not exist, regard shall be had to the following rules: (1) Joint tenancy, tenancy in common, joint property, common property or part ownership does not of itself create a partnership as to anything so held or owned, whether the tenants or owners do or do not share any profits made by the use thereof. (2) The sharing of gross returns does not of itself create a partnership, whether the persons sharing such returns have or have not a joint or common right or interest in any property from which or from the use of which the returns are derived. (3) The receipt by a person of a share of the profits of a business is *prima facie* evidence that he is a partner in the business, but the receipt of such a share, or of a payment contingent on or varying with the profits of a business, does not of itself make him a partner in the business; and in particular: (*a*) The receipt by a person of a debt or other liquidated amount by instalments or otherwise out of the accruing profits of a business does not of itself make him a partner in the business, or liable as such. (*b*) A contract for the remuneration of a servant or agent of a person engaged in the business by a share of the profits of the business does not of itself make the servant or agent a partner in the business,

first two of these rules, as Sir Frederick Pollock has pointed out, exclude "various relations of two or more persons to property held jointly or in common, and the returns derived from such property, which at first sight may appear to resemble partnership, but do not really satisfy the fundamental condition of 'carrying on a business in common with a view of profit.' As a matter of history, the conception of partnership has been worked out in our courts through the necessity of attending to distinctions of this kind." [1]

2. AMERICAN STATUTES. — Some of our States [2] have attempted to give similar legislative answers, although

or liable as such. (c) A person being the widow or child of a deceased partner, and receiving by way of annuity a portion of the profits made in the business in which the deceased person was a partner, is not by reason only of such receipt a partner in the business, or liable as such. (d) The advance of money by way of loan to a person engaged or about to engage in any business on a contract with that person that the lender shall receive a rate of interest varying with the profits arising from carrying on the business, does not of itself make the lender a partner with the person or persons carrying on the business, or liable as such. Provided that the contract is in writing, and signed by or on behalf of all the parties thereto. (e) A person receiving by way of annuity or otherwise a portion of the profits of a business in consideration of the sale by him of the good will of the business is not by reason only of such a receipt a partner in the business, or liable as such.

[1] Pollock's Digest of Partnership (5th ed.), 15, 16.

[2] In California, the Dakotas, and Montana, "Partnership," as defined by statute, "is the association of two or more persons for the purpose of carrying on business together, and dividing its profits between them." Cal. Code, § 2395. The Civil Code of Louisiana declares: "Partnership is a synallagmatic and commutative contract made between two or more persons for the mutual participation in the profits which may accrue from property, credit, skill, or industry, furnished in determined proportions by the parties." "Partnerships must be created by the consent of the parties." "A community of property does not of itself create a partnership, however that property may be acquired, whether by purchase, donation, accession, inheritance, or prescription." Arts. 2801, 2805, 2806. In New York, "a partnership, as between

none of these are quite as explicit or as carefully framed as those of the British statute. All are agreed to this extent, it is believed, that an association of persons is not a partnership, as between the members thereof, unless it is engaged in carrying on a business in common with a view of profit. And this statutory definition is but declaratory of the doctrine evolved by the courts, as will appear from an examination of typical cases in various jurisdictions.

3. PARTNERSHIP IS MORE THAN A COMMON ENTERPRISE. — Two carpenters, who join in a contract to do a piece of work for a third person, are not necessarily partners in the transaction. If their intention has not been expressed, it is to be inferred from their conduct. The fact that they immediately divide payments, instead of bringing them into a common fund with which new supplies are bought on joint account, indicates that they did not intend to form a partnership.[1] But when persons contract to manufacture machines, one supplying the patents and the others the money, "as long as the business shall prove practicable and profitable," although their written contract does not provide for a firm name and is silent as to the intention of the parties in forming this association, "the law makes it a partnership."[2]

4. PARTNERSHIP IS MORE THAN COMMON OWNERSHIP OF PROPERTY AND ITS RETURNS. — The relation existing between co-owners of lands and of chattels was a familiar one, and the body of rules regulating it was well defined,

the members thereof is the association, not incorporated, of two or more persons who have agreed to combine their labor, property, and skill, or some of them, for the purpose of engaging in any lawful trade or business, and sharing the profits and losses as such between them." L. 1897, ch. 420, § 2.

[1] Finckle *v.* Stacy, Macnaghten's Sel. Cas. in Chan. 9 (1725); Burdick's Cases on Part. 1; Dwinel *v.* Stone, 30 Me. 384 (1849); Burdick's Cases on Part. 17.

[2] Ill. Mall. Iron Co. *v.* Reed, 103 Iowa, 538; 71 N. W. 432 (1897).

long before English courts of justice were called upon to deal with the institution of partnership. Moreover, such co-owners were accustomed not only to hold the title to their property in common, but to share its income, — even to use it for the purpose of gaining a profit which they were to divide. An association of persons so using and enjoying their property bears a strong resemblance to a partnership. Two centuries ago, it is true, no one would have mistaken them for partners, because they were not merchants;[1] but now that partnership extends beyond merchandizing and includes "every trade, occupation, or profession,"[2] the distinction between co-owners and partners is not so broad and clear. However, if the evidence in a particular case establishes only such a relation between the common owners as was familiar to and regulated by the common law, it will not justify the inference that a partnership exists.

(*a*) *Examples of Common Ownership.* — Two persons buy a mill-site and jointly contract with a builder for the erection of a sawmill thereon. The only fair inference to be deduced from these facts is that the two are tenants in common.[3] To turn them into partners further proof must be adduced. If, in addition to the foregoing facts, it had appeared that these persons had sold an interest in the property to a third, who paid a part of the price in cash, and agreed that the balance should be paid out of his share of the profits to be made from running the mill, the inference that a partnership had been formed would have been warranted.[4] In the first case we have only a community

[1] *Cf.* Hammond *v.* Jethro, 2 Brownlow, 99 n. (1611); Burdick's Cases on Part. 245; which contains a judicial declaration that "two joynt shop-keepers are merchants."

[2] British Partnership Act of 1890, § 45.

[3] Porter *v.* McClure, 15 Wend. 187 (1836).

[4] Noyes *v.* Cushman, 25 Vt. 390 (1853).

of interest in real estate; in the latter we have the owners engaged in carrying on a milling business.

5. Part Owners of Ships. — Again, persons owning a ship in common are not, by reason of that fact alone, partners.[1] Indeed, it has been said by an eminent judge that the principle that persons do not become partners merely by becoming joint owners of a chattel and using it for a common purpose "is peculiarly applicable to ships or other craft, the exceptions to it in respect to them being always found in special circumstances."[2] But where several persons contracted for the construction and equipment of a ship for the purpose of "letting her to freight to the East India Company," they were considered partners, "it having been shown that this was their method of trading."[3]

6. Common Ownership of other Chattels. — We have seen that persons do not become partners by uniting in the purchase of a quantity of goods; nor do such buyers change their relationship by agreeing to hold the property with a view of selling it at an advance,[4] or with a view of using it in such a way as to produce a profit which they are to share.[5] Having acquired title to it as common law tenants in common, their subsequent dealings with it must go beyond the use which such owners could make of it within the pale of common law rules, and must disclose a mutual intention to carry on a business in common therewith. Such intention is shown very clearly when they buy a chattel for the purpose of employ-

[1] Helme *v.* Smith, 7 Bing. 709 (1831); Burdick's Cases on Part. 21.

[2] Hopkins *v.* Forsyth, 14 Pa. St. 34, 38 (1850).

[3] Doddington *v.* Hallett, 1 Ves. Sr. 497 (1751).

[4] Goell *v.* Morse, 126 Mass. 480 (1879); Burdick's Cases on Part. 23.

[5] French *v.* Styring, 2 C. B. N. S. 355 (1857); Burdick's Cases on Part. 22; Quackenbosh *v.* Sawyer, 54 Cal. 439 (1880); Burdick's Cases on Part. 25.

ing it in a business which they have agreed to carry on as partners.[1]

7. COMMON INTERESTS IN LAND. — Here, again, we have a relationship existing between co-proprietors which was not only familiar to the common law, but which it defined and regulated with abundant minuteness and technicality. Moreover, such real estate interests were not the ordinary subjects of merchandising. Indeed, as late as the year 1808, the Supreme Court of Massachusetts declared that "the law merchant does not extend to speculations in land," and that a person cannot be held to the liability of a dormant partner in such speculations.[2]

Although this doctrine has long been exploded, there appears to be no doubt that the courts are disposed to require stronger evidence of an intention on the part of common owners of real property to become partners than is required where chattels are the subject matter of co-proprietorship. Lord Thurlow went so far as to hold that an express contract between the owners was necessary in order to convert their title from that of joint tenants with the right of survivorship into that of partners.[3] This view was repudiated by Lord Eldon,[4] and no longer possesses any authority in England;[5] still, both in that country and in this, unless it is shown that real property has been acquired for and used in an established partnership business, it will be deemed to be owned by its associated proprietors, either jointly or in common; or, in the language of Lord Justice Lindley, it will be deemed

1 See Leiden v. Lawrence, 2 New R. (Exch.) 283 (1863).

2 Pitts v. Waugh, 4 Mass. 424 (1808). In Caines's Lex. Am. Merc. (1802), 424, it is said: "These fraternities must be restricted to chattel interests, for they cannot embrace real estate, as that would be to introduce a new species of tenure, unknown to the law of the land."

3 Thornton v. Dixon, 3 Brown's C. C. 199 (1791).

4 Townsend v. Devaynes, Mont. on Part. (1st ed.) Notes, p. 97 (1810).

5 Darby v. Darby, 3 Drewry, 495 (1856).

to be so owned, "unless there is some evidence to show that it has been treated by them as ancillary to the partnership business, and as part of the common stock of the firm."[1]

(*a*) *Modern Judicial Attitude.* — The following extract from a modern decision fairly represents the attitude of the courts upon this subject: "From its nature, and the legal requirements in regard to conveying title to it, real estate alone has rarely been the sole subject matter of a partnership. . . . From the nature of the property, the limitations of the agency of each partner in making a perfected sale, courts are not inclined to imply a partnership where the subject matter is real estate alone. Looking into these contracts, nothing is found indicative of a clear intention to form a partnership. No partnership, nor partnership name, nor partnership business, nor capital, is agreed upon. The parties agree to purchase certain property and fit it up for certain purposes, and to be at equal expense in doing it, and to share equally the profits that may arise from selling or leasing the property. They do not contemplate the carrying on of any business upon or in connection with the property so purchased. Each was in his own way to furnish his share of the funds necessary to accomplish the purposes of the contracts."[2]

[1] Lindley on Part. (5th Eng. ed.) 334; Jordan *v.* Soule, 79 Me. 590 (1887); Clark *v.* Sidway, 142 U. S. 682 (1891); Harris *v.* De Raismes, 56 N. J. Eq. —; 38 At. 637 (1897); Davis *v.* Davis (1894), 1 Ch. 393; Burdick's Cases on Part. 12.

[2] Farrand *v.* Gleason, 56 Vt. 633 (1884); Burdick's Cases on Part. 27. In Wheatley *v.* Calhoun, 12 Leigh (Va.) 264, 273 (1841), it is said: "Unless the intent of the joint owners to throw their real estate into the fund as partnership stock is distinctly manifested, or unless the real property is bought out of the social fund for partnership purposes, it must still retain its character of realty. Considering the partnership as a third person, the titles of the individual partners cannot be passed to it, perhaps, without violating the statute of frauds, unless it be by express agreement in writing, or unless by purchasing

On the other hand, if the contract shows that the parties have bought the land in common for the purpose of making it the very basis of a common business,[1] or if the business of the co-owners is such as necessarily to involve the land in its dealings, for example that of nursery gardening, where it is "practically impossible to separate the use of the soil for the trees and shrubs from the trees and shrubs themselves, which are a part of the freehold, and at the same time constitute the substantial stock in trade,"[2] the co-owners will be considered as holding the land in partnership.

(*b*) *Farming on Shares.*—The relation subsisting between the owner of land and a person farming it on shares was fixed at an early day as that of tenants in common of the crops.[3] Such is still not only the legal conception of their relationship, but the popular understanding as well. "Contracts of this nature," it has been judicially declared, "may either be regarded as a lease of the land, with a rent payable in a portion of the crop; or as an agreement by one man to work upon the land of another, and to receive a part of the crop as compensation for his labor; or as giving the laborer a qualified interest in the land"; [4] but "the proprietor and the occupant might be equally surprised to be informed that they were partners."[5]

with partnership funds an implied trust is raised in its favor." *Cf.* Partnership Act, § 20 (3): "Where co-owners of an estate or interest in land, . . . not being itself partnership property, are partners as to the profits made by the use of the land or estate, and purchase other land or estate out of the profits to be used in like manner, the land or estate so purchased belongs to them, in the absence of any agreement to the contrary, not as partners, but as co-owners."

1 State Nat. Bank *v.* Butler, 149 Ill. 575; 36 N. E. 1000 (1894).

2 Waterer *v.* Waterer, L. R. 15 Eq. 402 (1873).

3 Hare *v.* Celey, Cro. Eliz. 143 (1588).

4 Delaney *v.* Root, 99 Mass. 546, 549 (1868).

5 Donnell *v.* Harshe, 69 Mo. 170, 172 (1877); Burdick's Cases on Part. 30, *n.*

Undoubtedly it is quite possible for the parties so to frame their contract as to make them partners,[1] especially when they are joint owners of the land.[2] If the arrangement contemplates a joint title in the crops, their conversion into cash as a joint fund out of which advances are to be repaid, and that the balance is to be shared as net profits, it may fairly be inferred that a partnership was intended. A transaction of that character amounts to carrying on a business in common.

(c) *Managing and Improving Land.* — This is not treated by the courts as a business, ordinarily. A recent decision of the New York Court of Appeals has declared that a married woman was not carrying on a trade or business when managing her real estate, although she hired help to cultivate a part of it and rented other parcels. The statute enabling married women to carry on trade or business was interpreted as having "respect to business pursuits, — mechanical, manufacturing, or commercial."[3]

Perhaps this is a narrower definition of "business" than is to be found in any partnership adjudication or statute,[4] but it appears to accord fairly with the spirit of judicial and legislative deliverances on this topic. The dictum of Willes, J.,[5] that "if two tenants in common of a house agreed that one of them should have the gen-

[1] Reynolds *v.* Pool, 84 N. C. 37 (1881); Burdick's Cases on Part. 30, *n.*

[2] Fisher *v.* Sweet, 67 Cal. 228 (1885). *Cf.* Cherry *v.* Strong, 96 Ga. 183; 22 S. E. 707 (1895); Burdick's Cases on Part. 28.

[3] Nash *v.* Mitchell, 71 N. Y. 199 (1877).

[4] Partnership Act, § 45: Business includes "every trade, occupation, or profession."

[5] French *v.* Styring, 2 C. B. N. S. 355 (1857). *Cf.* Sir Frederick Pollock's comment: "But if they furnished the house at their joint expense, and then let portions of the house as lodgings, they might well be partners. Letting a house is not a business, but letting furnished rooms is." Digest of Part. (5th ed.) 3.

eral management, and provide funds for necessary repairs, so as to render the house fit for the habitation of a tenant, and that the net rent should be divided between them equally," they would not thereby become partners, has been accepted as a correct statement of the law, and is sustained by express decisions in this country.[1] In Sikes *v.* Work, cited in the last note, tenants in common bought a lot, on which a house was erected under the direction of the plaintiff. Later the plaintiff "carried on the business of keeping it as a boarding house, under an understanding between himself and the defendant that there should be a partnership between them" in the boarding house business; yet the court held that there was no partnership in the real estate. "There was no agreement between them to share the profit and loss of the joint undertaking, which is the essential and distinguishing feature of the contract of copartnership."

8. WITH A VIEW OF PROFIT. — Even though an association may possess business features, it is not necessarily a partnership. We have seen that the earliest form of partnership recognized by English law was that of joint merchants. It existed for the purpose of pecuniary gain. It was not a charitable, nor a benevolent, nor a moral reform institution. Naturally, therefore, there has been no hesitation on the part of courts in declaring that societies and clubs organized and maintained for the promotion of temperance,[2] for the enforcement of the laws,[3] for

[1] Sikes *v.* Work, 6 Gray (72 Mass.) 433 (1856). *Cf.* Noakes *v.* Barlow, 26 L. T. R. N. S. 136 (1872), where parties engaged in improving real estate were held partners because "every clause in the agreement showed that every act that was to be done, and every purchase that was to be made, was to be done or made in their joint names, for their joint benefit, and for both jointly," and the money used in paying for the improvements "was to be paid to a bank to their joint account."

[2] Lafond *v.* Deems, 81 N. Y. 507 (1880).

[3] McCabe *v.* Goodfellow, 133 N. Y. 89; 30 N. E. 728 (1892).

musical culture among their members,[1] for the propagation of political, social, or religious doctrines,[2] or even for mutual protection[3] or insurance,[4] are not partnerships, even though they may have for one of their objects the accumulation of property to be owned and enjoyed in common. It is not essential to the attainment of the objects which such associations have in view, that their members should severally possess the powers which the law merchant found it necessary to bestow upon each partner, such as the power of alienating firm property or of incurring firm obligations. Hence there is no foundation for a legal inference that the members of such associations possess those powers. On the other hand, it is uniformly held that the property rights and the legal liabilities of the members of these associations depend in the main upon their constitutions and rules.[5]

9. PROMOTERS ARE NOT PARTNERS. — The few cases in which the promoters of corporations, or the provisional committees for organizing business associations, have been declared to be partners,[6] are no longer entitled to consideration. These persons are not engaged in carrying on a business, but in preliminary negotiations for the

[1] Danbury Cornet Band *v.* Bean, 54 N. H. 524 (1874). Although this association is spoken of by Smith, J. as a partnership he admits that it might be considered an association of joint owners, and the property rights of its members are determined by the terms of their agreement, that is, by the association's by-laws, and not by the rules of partoership law.

[2] Flemyng *v.* Hector, 2 M. & W. 172 (1836); Richmond *v.* Judy, 6 Mo. App. 465 (1879); Queen *v.* Robson, 16 Q. B. D. 137 (1885).

[3] Caldicott *v.* Griffiths, 8 Exch. 898 (1853); Burt *v.* Lathrop, 52 Mich. 106 (1883); Brown *v.* Stoerkel, 74 Mich. 269 (1889), (Knights of Labor Assembly).

[4] Cohen *v.* N. Y. Mutual Life Ins. Co., 50 N. Y. 611 (1872).

[5] Ash *v.* Guie, 97 Pa. St. 493 (1881); Burdick's Cases on Part. 30.

[6] Holmes *v.* Higgins, 1 B. & C. 74 (1822); Lucas *v.* Beach, 1 Man. & G. 417 (1840).

launching of a business. They have no intention of acquiring the property rights or of exercising the contractual powers of partners.[1]

10. Agreements to form Partnerships. — While a true partnership cannot exist without a contract between its members, an association of persons does not become a partnership by the simple force of an agreement for that relationship. Partnership is more than a contract. Persons suing as partners do not make out a case by evidence that they have executed a written contract to carry on a business as partners. They must show that they carried on this business, and that their alleged cause of action accrued to them therein.[2] Nor will it matter that the parties have opened books of account, in which the existence of a partnership is recited and the interests of the various members are stated, nor that various steps have been taken preliminary to the opening of a firm business, nor that the refusal of any party to the contract to carry it into execution may subject him to a suit for damages by his repudiated associates. So long as the affair has not gone beyond a contract to carry on a business in the future, there is no partnership.[3]

### § 4. Joint Stock Companies.

(*a*) *Abnormal Partnerships.* — These associations were devised for the purpose of escaping certain consequences of an ordinary partnership, — especially the unlimited agency of each partner and his inability to devolve his

[1] Reynell *v.* Lewis, 15 M. & W. 517 (1846); Batard *v.* Hawes, 2 E. & B. 287 (1852); Burdick's Cases on Part. 33; West Point Foundry Asso. *v.* Brown, 3 Ed. Ch. 284 (1837).

[2] Gray *v.* Gibson, 6 Mich. 300 (1859).

[3] Martin *v.* Baird, 175 Pa. St. 540; 34 At. 809 (1896); Burdick's Cases on Part. 34; *cf.* Jackson *v.* Hennekenius, 5 Bro. P. C. 481 (1714); Hunnewell *v.* Willow Springs Canning Co., 53 Mo. App. 245 (1893), Opinion of Biggs, J.

partnership rights upon an outsider. In the language of an eminent English judge: "At first they existed under the favor of the Crown, which gave them charters of incorporation, and nobody ever supposed that the holders of stock in the Bank of England or the East India Company had anything to do with the law of partnership, or were partners. But there were large societies on which the sun of royal or legislative favor did not shine, and as to whom the whole desire of the associates and the whole aim of the ablest legal assistants they could obtain, were to make them as nearly a corporation as possible, with continuous existence, with transmissible and transferable stock, but without any individual right in any associate to bind the other associates, or to deal with the assets of the association."[1]

(*b*) *Their Legality fully established.* — After the passage of the famous South Sea Bubble Act,[2] the legality of these non-incorporated companies was doubted, notably by Lord Eldon.[3] Since the repeal of this statute, however, their legality at common law has been affirmed, Lord Cranworth declaring that "these companies, being consonant with the wants of a growing and wealthy community, have forced their way into existence, whether fostered by the law or opposed to it."[4]

Although the chartering of corporations is not, ordinarily, a matter of executive or legislative favoritism in this country, and joint stock companies are, therefore, less numerous than in Britain, their legality here has not been successfully challenged.[5] In the last cited case, it was

[1] In re Agriculturist Cattle Ins. Co., Baird's Case, 5 Ch. App. 725, 734 (1870).

[2] 6 Geo. I. c. 18.

[3] Van Sandan *v.* Moore, 1 Russ. 441, 472 (1826).

[4] Greenwood's Case, 3 DeG. M. & G. 459, 477 (1854).

[5] Phillips *v.* Blatchford, 137 Mass. 510 (1884).

charged that the company was formed to avoid having a paid up capital, which would have been necessary had a corporation been organized, and to escape taxation. But the court answered that the company was a partnership, and that if a partnership incurs debts the members are personally liable, and there is no need of paid up capital. Hence there was no wrong to the public; and, if persons choose to buy stock in such a concern, it is their own lookout.

(*c*) *No Delectus Personarum.* — One of the principal objects of the early partnership was the union of mercantile service and skill. In the quaint language of an old writer: "It may be that the one (partner) only conferreth the goods, and the other no goods, but bestoweth only his labor and diligence, which then is instead of goods. For labor is oftentimes of as good regard as money, yea, and sometimes much better, which causeth that even the poor, being industrious, may have fellowship with the rich."[1] The importance to the partner of the right to select as associates only such persons as, in his judgment, were possessed of the requisite business ability and skill, was enhanced by the mercantile custom that each partner was the unlimited agent of the firm. It was natural, therefore, for the law to assume that the ordinary partnership was "based on mutual trust and confidence of each partner in the skill, knowledge, and integrity of every other partner."[2]

The joint stock company, however, has in view the aggregation of capital rather than the union of personal talents. Not only are the owners of this capital so numerous that it is impracticable for all of them to take an active part in the conduct of the company's affairs, but by

[1] West's Symboleography, § 27 (1590).

[2] In re Agriculturist Cattle Ins. Co., Baird's Case, 5 Ch. App. 725, 733 (1870).

mutual agreement the business management is confined to a few persons, who may or may not be shareholders. In such circumstances, the ownership of shares may change, with the consequent withdrawal of old members and the introduction of new ones, without hazard to the owners of other shares. The personality of the ordinary member ceases to be important. It follows that these companies may provide that the withdrawal or death of a member shall not dissolve the association. Indeed, although the articles of association may be silent on this point, the presumption arising from the history, the nature, and the objects of these companies is that neither the death of a member nor the transfer of his shares works "a dissolution of the business."[1] The assignee or personal representative of a member may take the place of his predecessor, "on exactly the same terms and conditions as every other owner of a share, — equal benefit, equal liability."[2]

(*d*) *Liability of Shareholders.* — For the obligations of the company the shareholder's liability is that of the normal partner. It cannot be limited or modified by provisions in the articles of association. In the absence of legislative authority, stipulations for limited liability are "wholly nugatory as between the company and strangers," unless assented to by the latter.[3] Even the express declaration in the notes of a banking association, that they were to be paid by the members "out of their joint funds

[1] Carter *v.* McClure, 38 S. W. (Tenn.) 585 (1897); Burdick's Cases on Part. 37.

[2] In re Agriculturist Cattle Ins. Co., Baird's Case, 5 Ch. App. 725, 735 (1870).

[3] Walburn *v.* Ingilby, 1 My. & K. 61, 76 (1833), Brougham, L. C. It is to be borne in mind that, even in the case of normal partnerships, "there is nothing in the law to prevent a firm from stipulating with any creditor from the beginning that he shall look only to the members of the firm for the time being." Pollock's Digest of Part. (5th ed.) 58.

according to their articles of association," has been judicially declared not to be binding on the holders of the notes. "I see no reason to doubt," said Gibson, J., "but that they may limit their responsibility by an explicit stipulation made with the party with whom they contract, and clearly understood by him at the time. But this is a stipulation so unreasonable on the part of the partnership, and affording such facility for fraud, that unless it appears unequivocally plain, from the terms of the contract, I will never suppose it to have been in the view of the parties."[1]

(*e*) *Liability of the Estate and of the Representative of a deceased Shareholder.* — Although the personal representative of a shareholder may succeed to his membership in the company, and although the estate of the deceased may remain liable for the debts of the company contracted after his death, the personal representative is not bound to enter the association as a member; and until he does become "an actual partner in the concern,"[2] he will not be personally liable for its debts. Upon the death of a shareholder, the shares are vested in his personal representative, and the estate in such representative's hands is liable as a shareholder.

§ 4. (A.) **Defectively Incorporated Associations.**

(*a*) *Conflicting Doctrines.* — It is impossible to reconcile the different views concerning the liability of shareholders, in a defectively incorporated association, for its obligations. On the one hand it is maintained that as these associates intended that a business should be carried on with the capital which they contributed, in the manner

[1] Hess *v.* Werts, 4 S. & R. (Pa.) 356, 36 (1818).

[2] Wills *v.* Murray, 4 Exch. 843, 868 (1850). In this case becoming an actual partner involved the execution of the company's deed by the personal representative. Parke, B.

and by the agencies which they prescribed or assented to, and for their gain, they are partners, even though they did not intend to assume that relationship. On the other hand, it is declared that a partnership is never created between parties by operation of law, apart from an intention and agreement to constitute the relation; that where parties in good faith go through the form of organizing a corporation and the business is carried on in the name and by the agency of such apparent corporation, any intent to constitute the relationship is negatived. Let us consider the opposing arguments and authorities upon this topic.

(*b*) *Simulated Corporations are Partnerships.* — When the persons who own a business which is carried on for their gain pretend to be a corporation, without color of legality for their assumption, there is no difficulty in point of principle, and but little hesitation on the part of the courts, in treating them as partners.[1] Accordingly, if several persons subscribe and pay for shares in a banking institution, elect directors and officers, with the understanding that articles of incorporation are to be executed, and that all other steps are to be taken to legally organize the bank as a corporation, but no such steps are taken, the banking business carried on with such capital, and by such directors and officers, is that of a partnership.[2]

(*c*) *Business pending the Formation of a Corporation.* — Whether a business carried on while proceedings for the organization of a corporation are pending is that of a partnership, or not, will depend upon the facts of each case. If promoters of a contemplated corporation, after a

[1] Fuller *v.* Rowe, 57 N. Y. 23 (1874) · "That parties assuming to act in a corporate capacity without a legal organization as a corporate body are liable as partners to those with whom they contract, is not denied."

[2] McLennan *v.* Hopkins, 2 Kan. App. 260; 41 Pac. 1061 (1895); Burdick's Cases on Part. 41.

part of the stock has been subscribed for, believing that the scheme is to be successful, begin the business on their own credit, but agreeing to turn it over to the corporation as soon as it is organized, and no corporation is ever perfected, there is no partnership between these promoters and the stock subscribers.[1] Clearly the business thus carried on was the business of the promoters only. In case, however, the subscribers agree that a going business, in which they are all interested as proprietors, shall be carried on for their mutual profit until it is transferred to the corporation for whose stock they have subscribed, it will be a partnership business during the interim.[2]

(*e*) *Stockholders in De Facto Corporations.* — To constitute a *de facto* corporation, as distinguished from a corporation *de jure*, "there must be a law under which the incorporation can be had.[3] There must also be an attempt in good faith on the part of the incorporators to incorporate under such law," and there must be "an actual, open, and notorious exercise, unchallenged by the State, of the powers of a corporation."[4] When such an attempt has been made, but through some honest blunder the provisions of law have not been complied with, and consequently a *de jure* corporation has not come into existence, what is the liability of the stockholders for the obligations of the enterprise which is held out as a corporation by those responsible for it?

(*f*) *Liable as Partners.* — Undoubtedly they did not intend to form a partnership. Their principal object, in

[1] Ward *v.* Brigham, 127 Mass. 24 (1879); Rutherford *v.* Hill, 22 Ore. 218; 29 Pac. 546; 17 L. R. A. 549 (1892).

[2] Citizens' Bank *v.* Hine, 49 Conn. 236 (1881).

[3] Pope *v.* Capital Bank, 20 Kan. 440 (1878); Church *v.* Pickett, 19 N. Y. 482 (1859).

[4] McLennan *v.* Hopkins, 2 Kan. App. 260 (1895); Burdick's Cases on Part. 41.

undertaking to organize themselves into a corporation, was to limit their personal liability for the obligations of the business. And yet they intended to control, and do control, the business through persons whom they have selected, and the profits are and were intended to be theirs. It is true that they intended to create a legal entity, to vest the title to the property of the business in this entity, and to make it the debtor for all the obligations of the enterprise. Their exemption from personal liability for such obligations could be lawfully attained, however, in but one of two ways: by the assent of the creditors, or by legislative authority. If their enterprise is not a corporation *de jure*, clearly the proprietors of it have not secured legislative sanction for their coveted exemption. This was offered to them by the legislature upon their performance of specified conditions, which have not been performed. It would seem to follow, logically, that their common law liability has not been modified by legislative authority. It would seem, also, that the creditors have not assented to any modification of the common law liability of the stockholders, in cases where the latter have mistakenly represented that a corporation exists. These conclusions are sustained by a considerable body of judicial opinion.[1]

(*g*) *Not Liable as Partners.* — It must be admitted, however, that they do not accord with the weight of authority. The prevailing view appears to be, that, in cases where the stockholders have made a *bona fide* attempt to form a corporation, and the business has been carried on, honestly but mistakenly, as that of a corporation, the associates are not to be treated as partners, because "they never intended to form an association which the law calls a partnership."[2] In these cases, if

[1] See Bigelow *v.* Gregory, 73 Ill. 197 (1874).

[2] Parsons on Part. (4th ed.), § 57, and cases cited.

there is no corporate liability, the responsibility for the associate obligations rests upon the persons who take part in creating them,[1] and the title to the associate property has been held to vest in the persons who are acting as apparent agents of the association.[2]

(*h*) *Liability of Managers.* — Whether the responsibility of these persons is that of partners, or rests upon "an implied warranty of the corporate liability, analogous to the liability of one who assumes without authority to act as agent," or is "a liability imposed by statute," is a question upon which the courts are at variance.[3] The Supreme Court of Ohio has declared that such persons are liable as partners,[4] and this view prevails in Illinois.[5]

In Ridenour *v.* Mayo, the plaintiff sued the stockholders on a certificate of deposit, issued in the name of the Farmers' Savings Bank of Lima. Such a corporation had been organized by certain of the defendants, with a board of managers, president, treasurer, and cashier.

[1] Rutherford *v.* Hill, 22 Ore. 218; 29 Pac. 546; 17 L. R. A. 549 (1892).

[2] Fay *v.* Noble, 7 Cush. (61 Mass.) 188 (1851): "Fuller was not agent of a copartnership, for none existed; he was not the agent of individuals as such, because he was not authorized to act; he was not the agent of the Western Boston Iron Company, because, if the court were right in deciding that it had never been organized and that its proceedings were void, it never had the power to appoint him agent. Clearly then he acted without authority for any one. If he purchased, he purchased for himself. In him only did the property vest, and as against all but the vendors, he had the sole right to dispose of it to others."

[3] Parsons on Part. (4th ed.), § 57, approving Trowbridge *v.* Scudder, 11 Cush. 83 (1853); and Sullivan *v.* Sullivan Mfg. Co., 20 S. C. 79 (1883).

[4] Ridenour *v.* Mayo, 40 Ohio St. 9 (1883); *cf.* Morawetz on Private Corp. § 748.

[5] Loverin *v.* Laughlin, 161 Ill. 417 (1896): "The members or stockholders of a corporation, illegally formed, are liable as partners for its acts or contracts."

These managers, however, did not carry on a savings bank business, such as the incorporating statute permitted, but conducted a general banking business. They did business in the corporate name, but it was wholly *ultra vires.* The court said, "We are very clear that a partnership as to all was *prima facie* established, and that therefore the testimony as to the conduct and acts of each was properly received against all to strengthen the presumption."

# CHAPTER II.

## PARTNERSHIP AS TO THIRD PERSONS.

### § 1. Test of Sharing Profits.

WHILE the relationship of partners has never been imposed by the common law upon individuals, without their voluntary assent,[1] English courts held for a time, and some of our State courts still hold, that persons who participate in the profits of a business, are partners in such business as to third persons, although not partners as between themselves.[2]

1. EARLIEST STATEMENT OF DOCTRINE. — This doctrine was formally announced, for the first time, in the case of Grace *v.* Smith,[3] in these words: "Every man who has a share of the profits of a trade ought also to bear his share of the loss. And if any one takes part of the profit, he takes a part of that fund on which the creditor of the trader relies for his payment." The latter part of his opinion makes it clear that the Chief Justice was referring to one who shared the profits of a trade as a proprietor; who was a co-owner of the trade with the ostensible owner; to one on whose behalf the trade was conducted. He said: "I think the true criterion is to inquire whether Smith agreed to share the profits of the trade with Robinson, or whether he only relied on those profits as a fund of payment; a distinction not more nice than usually occurs in questions of trade and usury. The jury have said that this is not

[1] *Supra*, Chap. I. § 1.

[2] Gow on Part. (ed. of 1823), 11.

[3] 2 W. Bl. 998; Burdick's Cases on Part. 45 (1775), opinion of De Grey, Ch. J.

payable out of the profits, and I think there is no foundation for granting a new trial."[1]

If this limitation upon the doctrine had been observed and enforced, much "injustice and mischief" would have been avoided.

2. Doctrine Reaffirmed without Limitation. — Unfortunately, however, the reason assigned for the doctrine, rather than the limitation just referred to, impressed itself upon the judges in the leading case of Waugh *v.* Carver.[2] In that case Erasmus and William Carver, ship-agents at Gosport, entered into an agreement with Archibald Giesler, a ship-agent at Cowes, to allow each other certain portions of each other's commissions and profits, in consideration of mutual services to be rendered by each to the other. Plaintiff, having sold goods to Giesler at his agency in Cowes, brought suit for the price against the three as partners. Lord Chief Justice Eyre, delivering the unanimous opinion of the court, said: "It is plain upon the construction of the agreement, if it be construed only between the Carvers and Giesler, that they were not nor ever meant to be partners. They meant each house to carry on trade without risk of each other, and to be at their own loss. . . . But the question is whether they have not, by parts of their agreement, constituted themselves partners in respect to other persons. The case, therefore, is reduced to a single point, whether the Carvers did not entitle themselves and did not mean to take a moiety of the profits of Giesler's house, generally and in-

[1] Blackstone, J. rested his decision mainly on the fact that Smith was to receive from Robinson for the money furnished by the former five per cent and £300 per annum. "The hazard of the loss and profit," he reasoned, "is not equal and reciprocal, if the lender can receive only a limited sum for the profits of his loan, and yet is made liable to all the losses, all the debts contracted in trade, to any amount."

[2] 2 H. Bl. 235; Burdick's Cases on Part. 47 (1793).

definitely as they should arise at certain times agreed upon for the settlement of their accounts. That they have so done is clear upon the face of the agreement; and upon the authority of Grace *v.* Smith, he who takes a moiety of all the profits indefinitely shall, by operation of law, be made liable to losses, if losses arise, upon the principle that, by taking a part of the profits, he takes from the creditors a part of that fund which is the proper security to them for the payment of their debts."

(*a*) *Doctrine Originated with Lord Mansfield.* — The proposition that one who shares in the profits of a business "is, by implication and operation of law, clothed with the character of a partner" as to third persons, appears to have originated with Lord Mansfield. In Bloxham *v.* Pell,[1] cited by plaintiff's counsel in Grace *v.* Smith, and upon which "the judgment" in the latter case "appears to have been based,"[2] Lord Mansfield held that an agreement by which a retiring partner was to receive from the purchasing partner, who continued the trade as his sole business, a bond for £2,485, with five per cent interest on this amount and £200 per annum for six years, if the purchasing partner so long lived, as in lieu of the profits of the trade, "was a device[3] to make more than legal interest of money, and if it was not a partnership, it was a crime. And it shall not lie in the defendant Pell's (retiring partner's) mouth to say, 'It is usury and not a partnership.'" This view was referred to by the same great judge in a later case[4] as undisputed law. It was not only

1 2 Wm. Bl. 999 (1775); Burdick's Cases on Part. 45.

2 Lindley on Part. (5th ed.) *27.

3 This was clearly erroneous. The purchase price of Pell's interest was £2,485, the sum which Pell had contributed to the firm's capital, plus the annuity. The annuity was the agreed value of the accumulated profits and good will.

4 Hoare *v.* Dawes, 1 Doug. 371 (1780); Burdick's Cases on Part. 1.

followed in like cases,[1] so long as the usury statutes remained in force in England, but, by suggesting the doctrine which was laid down in Grace *v.* Smith and Waugh *v.* Carver, it introduced into partnership law "an amount of confusion which even the repeal of the usury laws failed to remove."[2]

3. Partnership Stipulations for Extra-Statutory Interest. — If a partnership actually exists, an agreement between its members that one shall receive more than the statutory rate of interest for capital contributed or money advanced by him to the firm, or that one shall pay to the firm more than statutory interest for money withdrawn by him, is not usurious. In the first case, the stipulation is for "an advantage to be taken out of the trade," which "may be measured in any way agreed on; for the money is not lying at interest, but employed in making profits subject to losses."[3] In the latter case, the agreement is not for a loan of money, but "in substance is to make a contribution to profits equal to the estimated earning power of the capital withdrawn and belonging in part to himself as one of the firm."[4]

If the parties did not contemplate a partnership, and the agreement does not result in the business being conducted

[1] It is true Lord Mansfield did not apply this doctrine consistently; *cf.* Morriset *v.* King, 2 Burr. 891 (1759); Jestons *v.* Brooke, Cowp. 793 (1778). In Morse *v.* Wilson, 4 D. & E. 353 (1791), Buller, J. seems to echo Lord Mansfield's heresy, that one who lends money to traders, and is to receive the statutory rate of interest *and* a share of the profits, is liable to the creditors of the business, although not a partner of the borrowers. Neither Kenyon, Ch. J., nor Ashurst, J., intimates any approval of this doctrine.

[2] Lindley on Part. (5th ed.) *16.

[3] Anderson *v.* Maltby, 2 Ves. Jr. 244 (1793); Fereday *v.* Howden, 1 Jac. 144 (1821); Gilpin *v.* Enderbey, 5 B. & Ald. 954 (1822); Cliff *v.* Barrow, 108 N. Y. 187 (1888); Burdick's Cases on Part. 93.

[4] Payne *v.* Freer, 91 N. Y. 43 (1883).

on behalf of the person advancing money, and stipulating for a share of the profits, in addition to the statutory rate of interest, as a compensation for its use, the transaction should be treated, and is generally treated, as that of a usurious loan.[1]

### § 2. Various Exceptions to the Old Rule.

An unsound legal rule breeds exceptions. Within three years after the decision of Waugh *v.* Carver, the same court decided[2] that a broker employed to sell goods, and to have for his own profit whatever sum he could get for them above a stipulated price, was not a partner of the owner. In the language of Justice Heath, "He must be considered as a broker, and not as a principal; he is only paid for his trouble in a particular manner."

(*a*) *A Sharer of Gross Returns is not a Partner.*—This was followed by cases holding that seamen, who receive a certain share of the produce of the cargo in lieu of wages, are not partners of the captain;[3] that the owner of a lighter is not a partner of the person who, in consideration of working the vessel, is to receive half the gross earnings;[4] that one pasturing bullocks is not a partner of their owner, although it is agreed that they shall equally share the excess above £20 received upon their sale;[5] that the captain of a ship who, in lieu of wages, primage, etc., is to receive one fifth of the profit and loss of the voyage, is not a

[1] Morse *v.* Wilson, *supra;* Arnold *v.* Angell, 62 N. Y. 508 (1875). In the latter case the agreement was for seven per cent interest on the money loaned and one quarter of the profits of the business. This, the Court of Appeals held, constituted usury.

[2] Benjamin *v.* Porteus, 2 H. Bl. 590 (1796); *cf.* Collom *v.* Bruning, 49 La. Ann. 1257; 22 So. 744 (1897).

[3] Wilkinson *v.* Frasier, 4 Esp. 182 (1803).

[4] Dry *v.* Boswell, 1 Camp. 329 (1808).

[5] Wish *v.* Small, 1 Camp. 333, *n.* (1808); *cf.* Stratton *v.* O'Connor, 34 S. W. 158 (1896); Burdick's Cases on Part. 61.

partner of the owners.[1] And thus the first exception to the rule was established that "a person who shares gross profits is not a partner."[2]

(*b*) *Receiving a Sum proportioned to Profits.* — Another exception to the rule, that one sharing in the profits of a trade became a partner by operation of law, is stated by Lord Eldon[3] in these words: "It is clearly settled, though I regret it, that if a man stipulates that as the reward of his labor he shall have, not a specific interest in the business, but a given sum of money, even in proportion to a given quantum of the profits, that will not make him a partner; but if he agrees for a part of the profits, as such, giving him a right to an account, though having no property in the capital, he is as to third persons a partner."[4]

This distinction, although not originally satisfactory to Lord Eldon, was accepted by the profession as simple and practical, and soon won approval from courts and jurists.[5] It became useless in England when the old rule was overthrown by the House of Lords in Cox *v.* Hickman,[6] but its influence survives there in the notion that persons may be

[1] Mair *v.* Glennie, 4 M. & S. 240 (1815); *cf.* Brown *v.* Hicks, 24 Fed. 811 (1885).

[2] Heyhoe *v.* Burge, 9 C. & B. 431 (1850), Parke, B.

[3] Ex parte Hamper, 17 Ves. 403 (1811).

[4] Lord Eldon has been called "the great enforcer of this distinction." Lindley on Part. (5th ed.) *29. He appears to have given to it its authoritative, if not its earliest judicial sanction.

[5] Story on Part. (5th ed.), §§ 33 to 36. Lord Bramwell, referring to Story's approval of this distinction as satisfactory, asks: "Satisfactory in what sense? In a practical business sense? No; but in the sense of an acute and subtle lawyer, who is pleased with refined distinctions, interesting as intellectual exercises, though unintelligible to ordinary men, and mischievous when applied to the ordinary affairs of life." Bullen *v.* Sharp, L. R. 1 C. P. 86 (1865); Burdick's Cases on Part. 71.

[6] 8 H. L. Cases, 268 (1860).

partners in the profits of a business, although not partners in the business itself.[1] In this country it is still a live and mischievous doctrine in not a few jurisdictions. It is admittedly difficult of application,[2] and has been rejected by many of our courts as "unimportant and merely verbal," [3] as well as "an arbitrary one, resting on authority and not principle." [4]

(*c*) *Sharing the Profits as Such.* — The courts which continue to enforce this distinction are careful to say that the share of the profits which is to be taken must be a "proprietary interest," "an interest in the profits as such," "a right to insist upon an accounting and a division thereof" at definite periods.[5] If they meant by this language that a person who stipulates for and receives a share of the profits of a business, in which he is a common proprietor with those who carry it on, should be liable as a partner, although he pretends to be a creditor only of the business, no fault could be found with the statement. In such a case, the business would be carried on in common by him and its ostensible owners. To call the share of the profits for which he has stipulated a compensation for his services, or for the use of his property, would be a subterfuge. Such, however, is not the meaning of these tribunals.

(*d*) *Doctrine of Leggett v. Hyde.* — This is apparent from the able opinion in the case last cited. The defendant Hyde loaned to the firm of A. Putnam & Co. $2,000 for one year, in consideration of which Putnam & Co. agreed to hire Hyde's son as clerk, at $10 per week for

[1] Lindley on Part. (5th ed.), *14, and cases cited.

[2] Cox *v.* Delano, 3 Dev. L. (N. C.) 89 (1831).

[3] Beecher *v.* Bush, 45 Mich. 188 (1881), Cooley, J.

[4] Dunham *v.* Rogers, 1 Barr. (Pa.) 255 (1845), Gibson, C. J.

[5] Leggett *v.* Hyde, 58 N. Y. 272 (1874); Burdick's Cases on Part. 50.

the year, to pay Hyde one third of the profits, which were to be settled half yearly, and at the end of the year to take him in as a partner if the firm and he should feel satisfied, upon his supplying more money. Hyde never interfered in the affairs of the concern, nor exercised any control of the business; nor had he any right to interfere, to transact business, or to sign for the firm or to bind the same. The court did not intimate that Hyde had any proprietary interest in the business. "It matters not," said the court, "that the defendants meant not to be partners at all and were not partners *inter sese*." Inasmuch as Hyde obtained "an interest in the profits, as such, and a right to insist upon an accounting and a division thereof half yearly," he was declared to be a partner as to third persons, since he had a right to take "a part of the fund which in great measure is the creditor's security for the payment of debts to them," although in fact he "never received anything for his $2,000, nor anything by way of interest money."

In other cases decided by the same court, parties who had the right to take, and did take, a part of this same sacred fund were held not to be partners, even as to third persons, because their "interest in the profits" was "as a compensation for the money loaned." [1]

**§ 3. The Test of Intention.**

With the growth of exceptions to the rule, doubts sprang up as to the soundness of the rule itself. The test of partnership which it furnished was recognized as artificial, and its enforcement was found to be productive of great hardship and injustice. [2] In the cases which first

[1] Richardson *v.* Hughitt, 76 N. Y. 55 (1879), and other cases as digested by Ruger, Ch. J., in Hackett *v.* Stanley, 115 N. Y. 625 (1889); Burdick's Cases on Part. 57, 60.

[2] Weiss *v.* Weiss, 166 Pa. St. 490; 31 At. 247 (1895); Burdick's

declared exceptions to the rule, the judges laid stress upon the facts that the parties never intended to form a partnership, and that such a relation between them was inconsistent with the business usages in those branches of trade. To hold that a broker was a partner of his employer, or that seamen were partners of their captain, was to do violence to the intention of the parties, as well as to the understanding of the business community.[1] English courts, true to their judicial habit, distinguished these cases from Waugh *v.* Carver, instead of overruling it; content to be practical rather than logical. However, the reasoning in these very cases led inevitably to the adoption of a new test of partnership.

1. Cox *v.* Hickman. — The first authoritative statement, in England, of the new test appeared in the judgments delivered in the House of Lords in Cox *v.* Hickman.[2] Creditors of an embarrassed partnership (B. Smith and Son) entered into a deed of arrangement with the firm, by which the firm property was assigned to certain trustees, who were to carry on the business under the name of the Stanton Iron Company; to divide the net income among the creditors in ratable proportions, and, after the debts were discharged, to retransfer the property to the Smiths. The creditors had the right to make rules for the conduct of the business, or to put an end to it, but the property and its income were to be deemed the property of the Smiths. Hickman, who had supplied goods to the business and received therefor bills accepted by the trustees in the name of the Stanton Iron Company, sought to hold all of the creditors who had executed the deed as partners.

Cases on Part. 55, 56; Mollow, March, & Co. *v.* Court of Wards, L. R. 4 P. C. 419 (1872).

[1] *Supra*, p. 41.

[2] 8 H. L. Cas. 268 (1860); Burdick's Cases on Part. 65.

Clearly, under the doctrine of Waugh *v.* Carver, they were liable to Hickman as partners. They were to receive a share of the profits as such. Just as clearly, the creditors did not intend to enter into the relation of partnership. The claim of one creditor, the Midland Railway Company, amounted to only £39, "and to suppose that the directors could imagine that they were making themselves partners" was considered "absurd." Moreover, such deeds of arrangement were of frequent occurrence, and yet neither lawyers nor business men supposed they created a partnership. By a case of this character, the arbitrariness and hardship of the old rule were fully disclosed. Although the judges in the Exchequer Chamber, as well as those who were summoned to the House of Lords during the argument, were equally divided as to the proper decision of the case, — some of them believing that the doctrine of Waugh *v.* Carver "had become so inveterately part of the law of England that it would require legislation to reverse it," [1] — their Lordships were unanimous in holding that the creditors were not partners.

(*a*) *Reasons for the Decision.* — While their Lordships were not entirely agreed, nor entirely clear,[2] in the reasoning which led up to their unanimous conclusion, and while the emphasis which they laid upon agency as a test of partnership was unfortunate,[3] the *ratio decidendi* of the case is found in the following extract from Lord Cranworth's judgment: "It is often said that the test, or one of the tests, whether a person not ostensibly a partner is, nevertheless, in contemplation of law, a partner, is

[1] Lord Blackburn in Bullen *v.* Sharp, L. R. 1 C. P. 86 (1865).

[2] "For some time" the consequences of Cox *v.* Hickman "were still imperfectly understood, even by some of the noble and learned persons who had taken part in the decision." Pollock on Part. (5th ed.), 17.

[3] Gray, J., in Meehan *v.* Valentine, 145 U. S. 611 (1892); Burdick's Cases on Part. 80, 82.

whether he is entitled to participate in the profits. This, no doubt, is in general a sufficiently accurate test; for a right to participate in profits affords cogent, often conclusive, evidence that the trade in which the profits have been made was carried on in part for, or on behalf of, the person setting up such a claim. But the real ground of the liability is, that the trade has been carried on by persons acting on his behalf. When that is the case, he is liable to the trade obligations, and entitled to its profits, or to a share of them. It is not strictly correct to say that his right to share in the profits makes him liable to the debts of the trade. The correct mode of stating the proposition is to say that the same thing which entitles him to the one makes him liable to the other; viz., the fact that the trade has been carried on on his behalf, i. e. that he stood in the relation of principal towards the persons acting ostensibly as the traders, by whom the liabilities have been incurred, and under whose management the profits have been made."

(b) *The Present English Rule.* — Substantially in accordance with the foregoing extract is the present English rule, as it appears in sections one and two of the Partnership Act.

It should be noted, however, that the third section of that Act postpones the rights of one who is to receive a rate of interest varying with the profits, or a share of the profits as compensation for a loan of money,[1] as well as the rights of one who is to receive a portion of the profits in consideration of the sale by him of the good will of the business, in case of insolvency of the debtor, until the claims of other creditors have been satisfied.[2]

[1] Section two requires a contract of this kind to be in writing. *Cf.* Pennsylvania statute, referred to in Weiss *v.* Weiss, 166 Pa. St. 490 (1895); Burdick's Cases on Part. 55.

[2] Sir Frederick Pollock, referring to the statute for which this sec-

(c) *Dissolution of the Old Rule.* — In deciding Cox *v.* Hickman, the House of Lords did not formally overrule Waugh *v.* Carver. Indeed, one of the noble lords undertook the difficult task of justifying the conclusion reached in that case, while repudiating the reasons upon which it was based. The judgment in Cox *v.* Hickman, however, did overrule the notion that "he who takes a moiety of all the profits indefinitely shall by operation of law be liable to losses," — one which Lord Bramwell declared had "caused more injustice and mischief than any bad law in our books";[1] or in the more conventional phrase of Sir Montague Smith, "the judgment had certainly the effect of dissolving the rule of law which had been supposed to exist, and laid down principles of decision by which the determination of cases of this kind is made to depend, not on arbitrary presumptions of law, but on the real contracts and relation of the parties."[2]

tion is in part a substitute, has said: "The Act was meant to do away with the hardship of the unqualified rule that whoever shared the profits of a business was liable as a partner. But that supposed rule (as now appears) was in fact abrogated by the decision in Cox *v.* Hickman, and the Act expressed only a part of the new footing on which the law was thus placed. Parliament intended to produce a substantial amendment of the law, and produced unawares a stray bit of codification. As an acute and plain spoken judge has since said, the effect of Cox *v.* Hickman was not understood at the time. The singular part of the story is that the misunderstanding was shared by the law officers of the Crown, all the law lords (two of whom had been parties to the decision in Cox *v.* Hickman), and, it would seem, the legal profession generally. Whence the moral may be drawn that the evolution of law by the unaided natural process of litigation is an even more subtle and excellent thing than one would imagine, seeing that, as in this case, it may take not less than five years for a leading judgment of the ultimate Court of Appeal to be felt in its full extent." Essays in Jurisprudence, 83.

[1] Bullen *v.* Sharp, L. R. 1 C. P. 86 (1865); Burdick's Cases on Part. 71, 76.

[2] Mollow, March, & Co. *v.* Court of Wards, L. R. 4 P. C. 419 (1872).

2. American Courts had anticipated the House of Lords. — These principles of decision had been laid down by courts in this country some time before the judgment in Cox *v.* Hickman. In many of the States,[1] unfortunately, the courts of last resort had adopted the doctrine of Waugh *v.* Carver, before its unsoundness and injustice were fully appreciated; but in others it had been greatly modified[2] or squarely rejected.[3]

The Supreme Court of Tennessee, in the case last cited, declared that, as there was no decision in that State upon the point, it would "not admit the doctrine that the mere participation in the profits of a business, whether gross or net profits, is to be taken as conclusive of a partnership, even in favor of creditors, irrespective of the truth of the case," but would "proceed upon the more just and sensible view that participation in the profits affords merely a presumption, which is to prevail only in the absence of proof to the contrary; and that it is a question of fact, upon inquiry and proof, whether the circumstances under which the participation in the profits exists clearly demonstrate that the profits are taken, not in the character of partner, but in a totally different character, and merely as compensation for services or benefits rendered by the person by whom they are received."

This has become the prevailing view in our State and Federal courts.[4]

3. Executor of a Deceased Partner. — In Waugh *v.* Carver, the Chief Justice expressed the opinion that that

[1] Leggett *v.* Hyde, 58 N. Y. 272 (1874); Burdick's Cases on Part. 50; Weiss *v.* Weiss, 166 Pa. St. 490; Burdick's Cases on Part. 55, citing early cases in those States.

[2] Holmes *v.* Old Colony Ry., 5 Gray (71 Mass.) 58 (1855).

[3] Polk *v.* Buchanan, 5 Sneed (Tenn.) 721 (1857); Burdick's Cases on Part. 61.

[4] Meehan *v.* Valentine, 145 U. S. 611 (1892); Thillman *v.* Benton, 82 Md. 64 (1895); Burdick's Cases on Part. 80, 85.

case would not lead to the "consequence that, if there was an annuity granted out of a banking house to the widow, for instance, of a deceased partner, it would make her liable for the debts of the house." Later, however, it was decided that the executor of a deceased partner, who continued his share in the business for the benefit of his infant child, was liable as a partner;[1] and still later, that the *cestui que trust* was also liable.[2] But this view no longer obtains either in England or here.

The executor may become a partner, by voluntarily taking the place of the deceased in the firm with the assent of the survivors, but he does not incur the liabilities of a partner by permitting the deceased's share to remain in the business, and by receiving for the use thereof a share of the profits.[3] He is not obliged to take the risks of a partner, simply because his testator has directed that the share shall be continued in the business. In case the partnership articles provide that the testator's capital shall remain in the business, the executor cannot withdraw it without subjecting the estate to liability to suit; and the capital so remaining is liable for the debts of the business.

The executor, however, incurs no personal liability, unless he voluntarily assumes the relationship of partner. If he does so enter the partnership, in compliance with his testator's directions, and thus take upon himself personal responsibility for the firm's debts, he will be entitled to indemnity out of the testator's estate to the extent of the fund embarked in the business by the will. Beyond this, any loss must be his own.[4] Such a partner occupies an

[1] Wightman *v.* Townroe, 1 M. & S. 412; 4 Taunt. 412 (1813).

[2] Goddard *v.* Hodges, 1 Cr. & M. 33 (1832).

[3] Holme *v.* Hammond, L. R. 7 Ex. 218 (1872).

[4] Wild *v.* Davenport, 48 N. J. L. 129; 7 At. 295 (1886); Burdick's Cases on Part. 77.

unenviable position. He can never bag the profits, and may be compelled to pocket the losses.

4. Desire to Escape Partnership Liabilities. — While the true test of partnership is the intention of the parties, the inquiry concerning that intention is not to be limited to the language of their agreements; nor is this intention to be confounded with the desire to escape the liabilities of a partner while stipulating for the rights and benefits of that relationship. Every provision of the agreement and all the circumstances of the case are to be considered in determining whether a partnership has been entered into. If the business carried on under their agreement is owned jointly by them, and is carried on for their benefit as proprietors, however explicitly they may declare that one is a lender and the other a borrower, or however elaborate their devices or ingenious their contrivances for concealing their true relationship, the courts will declare them partners.[1]

5. Sharing both Profits and Losses. — The opinion has been expressed by a learned author that "persons engaged in any trade, business, or adventure, upon the terms of sharing the profits *and* losses arising therefrom, are necessarily to some extent partners in that trade, business, or adventure."[2] It is not borne out by the authorities, however, either in England or in this country. Whether parties who stipulate to bear the losses as well as to share the profits of a business venture are partners or not, depends upon the further question whether they are jointly interested in the venture as co-proprietors. If the parties enter into an agreement of this character "in order to avoid conflict and rivalry between them" in a particular

[1] Pooley *v.* Driver, 5 Ch. D. 458 (1876); Merrall *v.* Dobbins, 169 Pa. St. 480; 32 At. 578 (1895); Burdick's Cases on Part. 86.

[2] Lindley on Part. (5th ed.), *10. See opinion of Lindley, L. J., in Walker *v.* Hirsch, 27 Ch. D. 460 (1884); Burdick's Cases on Part. 90.

trade,[1] or if its design is "to induce care on the part of" one who is really agent for the other contracting party,[2] no partnership is created.

On the other hand, a partnership may exist between persons who have contracted for that relationship, although they have agreed that one shall keep the other "harmless from all losses, debts, dues, or demands that may come against the firm."[3] This doctrine, it is true, has been disputed in a few jurisdictions.[4] In the case last cited it is declared that in this country "the general doctrine is that, in order to constitute general partnership as between the partners, there must be some kind of liability for the losses of the concern. Indeed, it is difficult to see how one can be a partner in, — can participate in, and be partner of a business, — without being subject to those fortunes." The court, however, did not question that the party guaranteed against loss might be liable to third persons as a partner by estoppel.

### § 4. Partner by Estoppel.

While a true partnership exists only where the parties have agreed to create that relationship, a person may subject himself to the liabilities of a partner without possessing a partner's rights. If he holds himself out, or permits others to hold him out, as a partner in a business, he will not be allowed to deny this representation as against those who have acted in reliance upon its truth.

(*a*) *Not a Partner "to the World."* — Lord Mansfield

[1] Clifton *v.* Howard, 89 Mo. 192 (1886); Burdick's Cases on Part. 88.

[2] Canton Bridge Co. *v.* City of Eaton Rapids, 107 Mich. 613; 65 N. W. 761 (1895); Burdick's Cases on Part. 90.

[3] Clift *v.* Barrows, 108 N. Y. 187 (1888); Burdick's Cases on Part. 93.

[4] Winter *v.* Pipher, 96 Iowa, 17 (1895); Burdick's Cases on Part. 90, *n.*; Whitehill *v.* Shickle, 43 Mo. 537 (1869).

is reported to have said that, as the defendant "suffered her name to be used in the business, and held herself out as a partner, she was certainly liable, though the plaintiff did not, at the time of dealing, know that she was a partner, or that her name was used"; [1] and Chief Justice Eyre declared that, if one "will lend his name as a partner, he becomes, as against all the rest of the world, a partner." [2]

This doctrine has been modified by subsequent decisions in England. As early as 1829, Mr. Justice Parke laid down the rule that when a plaintiff seeks to subject one who is not in reality a partner to a partner's liability, he must show that the defendant "had held himself out to be a partner, not 'to the world,' for that is a loose expression, but to the plaintiff himself, or under such circumstances of publicity as to satisfy a jury that the plaintiff knew of it and believed him to be a partner." [3] Under this rule, the liability of one holding himself out to be a partner "is nothing more than an illustration of the general principle of estoppel by conduct." [4]

(*b*) *A few Discordant Decisions.* — While the great body of judicial authority [5] in this country accords with the rule stated above, a few learned judges [6] have announced their preference for Lord Mansfield's view. In Poillon *v.* Secor the court declared: "The sound rule would seem to be, that a person who deliberately agrees

[1] Young *v.* Axtell (1784), cited in Waugh *v.* Carver, 2 H. Bl. at p. 242.

[2] Waugh *v.* Carver, *supra;* Burdick's Cases on Part. 47, 48.

[3] Dickinson *v.* Valpy, 10 B. & C. 128 (1829).

[4] Lindley on Part. (5th ed.), *40.

[5] Thompson *v.* First Nat. Bank, 111 U. S. 530 (1884); Burdick's Cases on Part. 96.

[6] Dwight, C., in Poillon *v.* Secor, 61 N. Y. 456 (1875). (The statement quoted by the learned judge, in support of his view, from the second edition of Parsons on Partnership, has been omitted from the fourth edition.) Holmes, J., in Bartlett *v.* Raymond, 139 Mass. 275 (1885).

that his name shall be used in a partnership must be conclusively presumed to intend the consequences which naturally flow from such an act. It would be contrary to public convenience to require affirmative proof that dealers with the firm knew who was represented by the fictitious name." This view, that the liability of one holding himself out as a partner rests upon considerations of public policy rather than upon principles of equitable estoppel, was thought to be strengthened by a New York statute making the use of fictitious partnership names a crime.

The court expressed its approval of the following distinction, suggested by a distinguished writer: "Where one is held forth to the world as a partner . . . by his authority, consent, or connivance, the presumption is absolute that he was so held out to every creditor or customer. If so held out by his own negligence only, he should be held only to a creditor who had been actually misled thereby."[1]

1. Nominal Partner as a Party Litigant. — As a nominal or holding-out partner is liable only on the ground of estoppel, and not because he is one of the contracting parties in transactions relating to the business of the ostensible firm, he need not be a party to litigations growing out of such transactions. He need not join as a plaintiff. "A party with whom the contract is actually made may sue without joining others with whom it is apparently made."[2] Nor is it necessary to make him a defendant. The plaintiff may waive his right against him, and sue only the actual owner of the business.[3]

If he is made a defendant, however, it must be in his assumed capacity as partner. The liability which he is estopped to deny is that of a joint promisor with those per-

[1] Parsons on Part. (2d ed.), 119.

[2] Kell v. Nainby, 10 B. & C. 20 (1829).

[3] Hatch v. Wood, 43 N. H. 633 (1862).

sons whom he has held out as his partners. Accordingly, where A. retires from the firm of B. & Co., and B., the continuing partner, enters into partnership with C., the new firm carrying on business in the old name, A. will be liable jointly with B. on contracts of the new firm made with persons who have not been duly notified of the change. By permitting the business to be carried on in the old name, without notice of his retirement, he virtually represents that the old partnership continues. He is not liable jointly with B. and C., however, for he never has held himself out as their partner; nor is he severally liable to a customer who, after notice of the change in the partnership, has elected to take the new firm as his debtors.[1] Undoubtedly, a partner who has retired from a firm may be jointly liable with the members of the new firm on its contracts; but only in cases where his conduct has led the creditors to believe that he was a member of the new firm when the contracts were made.[2]

2. Holding Out, a Question of Fact. — Whether a person has held himself out to be a partner is a question of fact. It is not strange, therefore, that different juries, upon the same evidence, have given different answers to the question whether the defendant had held himself out as a partner in a particular business.[3] If there is no conflict of evidence, and but one inference can reasonably be drawn therefrom, the question will be answered by the court.[4]

[1] Scarf *v.* Jardine, 7 App. Cas. 345 (1882); Burdick's Cases on Part. 101. Mr. James Parsons's criticism of this case is based upon a misapprehension of its doctrine. Parsons's Principles of Part., § 70.

[2] Thayer *v.* Goss, 91 Wis. 90; 64 N. W. 312 (1895); Burdick's Cases on Part. 102.

[3] Wood *v.* Duke of Argyll, 6 M. & Gr. 928 (1844); Lake *v.* Duke of Argyll, 6 Q. B. 477 (1844).

[4] McClewee *v.* Hall, 103 N. Y. 639 (1886); Harris *v.* Sessler, (Tex.) 3 S. W. 316 (1887).

(*a*) *What Amounts to Holding Out?* — Perhaps no better answer, in general terms, can be given to this question than that which is furnished by the British Partnership Act: "Every one who by words spoken or written, or by conduct, represents himself, or who knowingly suffers himself to be represented, as a partner in a particular firm, is liable as a partner to any one who has, on the faith of any such representation, given credit to the firm, whether the representation has or has not been made or communicated to the person so giving credit by or with the knowledge of the apparent partner making the representation, or suffering it to be made."[1]

3. NOTICE BY RETIRING PARTNER. — Although a member of a firm retires from the business, he may remain liable as a holding-out partner, unless proper notice of his retirement is given.[2] The rule is formulated in the British statute as follows: "Where a person deals with a firm after a change in its constitution, he is entitled to treat all apparent members of the old firm as still being members of the firm, until he has notice of the change."[3]

This notice, in the case of former dealers, must be an actual one,[4] although it is not necessary that it be communicated directly by the retiring partner to such dealers.[5]

[1] § 14, (1). The second subsection provides that this rule shall not apply to the estates of a deceased partner. Such is the settled law. See Marlett *v.* Jackman, 3 Allen (Mass.) 257 (1861); Burdick's Cases on Part. 547.

[2] *Supra*, p. 52.

[3] Partnership Act, 1890, § 36 (1). The second subsection provides for advertisements in the London Gazette, the Edinburgh Gazette, and the Dublin Gazette. The third subsection recognizes the established exception in favor of the estate of a deceased, a bankrupt, or of a dormant partner.

[4] Austin *v.* Holland, 69 N. Y. 571 (1877). A notice mailed to a former dealer, but not received, does not protect the retiring partner.

[5] Gathright *v.* Burke, 101 Ind. 590 (1884); Potter *v.* Tolbert, (Mich.) 71 N. W. 549 (1897); Burdick's Cases on Part. 367.

As to all other persons, a public notification, generally by advertisement in a newspaper "circulated in the locality in which the business of the partnership has been conducted,"[1] is sufficient. It is to be borne in mind that no particular form of notice is required. Inasmuch as the defendant's liability, in cases now under consideration, rests upon an equitable estoppel, any evidence which shows that the plaintiff had no reasonable ground for reliance upon the defendant's membership in the firm is admissible.[2]

4. WHO ARE FORMER DEALERS? — Not every business transaction with a firm will bring a party within this class. If it is one which would not reasonably be attended by any trust reposed in or credit given to the members of the firm, the other party to the transaction is not considered a dealer,[3] who is entitled to actual notice of a change in its membership. Hence one who has sold goods to a firm on credit, even though no definite time of forbearance is agreed upon, is a former dealer, but one who has sold only for cash is not,[4] nor is one who has been a purchaser only from the firm.[5]

Again, it would be unreasonable to require actual notice to be given to persons whose identity and address are not brought home to the partnership. Accordingly, one who has bought the firm's paper from third persons, without request from the firm or negotiations with it, is not entitled to actual notice.[6]

1 Askew *v.* Silman, 95 Ga. 678 ; 22 S. E. 573 (1895) ; Burdick's Cases on Part. 106.

2 Cases cited in last two notes.

3 Vernon *v.* Manhattan Co., 22 Wend. (N. Y.) 183 (1839).

4 Clapp *v.* Rogers, 12 N. Y. 283 (1855). In this case, Hand, J. said, "The credit on the faith of the partnership, mentioned by some writers, I suppose to mean confidence in the solvency and probity of the firm, and not necessarily an agreement for the forbearance of some debt."

5 Askew *v.* Silman, *supra.*

6 City Bank *v.* McChesney, 20 N. Y. 240 (1859).

5. USING OLD FIRM NAME AFTER NOTICE OF DISSOLUTION. — This, if done with the assent of the retiring partner, will render him liable for the debts of the new business.[1] It is clear that such should be its effect, where the retiring partner informed the plaintiff that, although he had ceased to be a partner, his name was to continue for a certain time.[2] Here, certainly, was a representation of his willingness that the plaintiff should deal with the firm on the credit of all of its old members.

However, it has recently been held in England that, if due notice of the dissolution of a firm has been given, the retiring partner will not be liable to creditors of the continuing partner, although the former permits the latter to carry on business in the old name.[3] Permission "to carry on the business under the old firm name," it was said, did not "amount to a representation" by the retired partner "that he was a partner in the firm."

(a) *Use of Old Name by a New Firm.* — This also may subject those who have sold out their business to strangers to the liability of partners in the new firm.[4]

5. QUASI PARTNER'S LIABILITY FOR TORTS. — The liability of a true partner for the torts of his copartners will be discussed in a subsequent chapter. It may be stated in general terms, however, that he is liable for all torts committed by his authority, or by his copartners, or by the firm's agents, acting in the ordinary course of the firm's business.[5]

[1] Re Kreuger, 2 Lowell, 66 (1871).

[2] Brown *v.* Bush, 2 Chitty, 120 (1816); *cf.* Alderson *v.* Pope, 1 Camp. 404, *n.* (1809), and comments thereon in Collyer on Part., Wood's ed. 38; Willis *v.* Rector, 50 Fed. 684 (1892).

[3] In re Fraser (1892), 2 Q. B. 633; Burdick's Cases on Part. 108.

[4] Evans & Howard Co. *v.* Hadfield, 93 Wis. 665; 68 N. W. 468 (1896); Burdick's Cases on Part. 110. "The defendant should have foreseen that this use of his name was well suited to give the impression that he was the leading partner in the new firm."

[5] British Part. Act of 1890, § 10.

A quasi partner's liability for firm torts is less extensive. He is answerable in a tort action for deceit, undoubtedly, where the person whom he held out as his partner has induced third parties by false representations concerning quality to buy firm property to their damage.[1] But, as his responsibility for firm transactions rests solely on estoppel, he is not answerable in tort to third persons who have been injured by the negligence of an agent of the firm. His holding himself out as a partner does not induce the third person, in such a case, to change his position to his detriment. A ruling to the contrary by a distinguished English judge is reported;[2] but it was made while Lord Mansfield's heresy of Young *v.* Axtell was in vogue, and has been thoroughly discredited.[3]

6. Rights of Creditors against the Property of a Partner by Estoppel. — Not only may a person estop himself from denying that he is a partner in a business, but "by permitting his property to be used and held out as the property of a partnership, he may make that property liable for the debts of the partnership."[4] Accordingly, one who holds himself out as in partnership with another cannot have any of the business assets set off to him under an exemption statute, although all the assets are his separate property, and the pretended copartner is his minor son.[5]

[1] Sherrod *v.* Langdon, 21 Iowa, 518 (1866); Burdick's Cases on Part. 112; *cf.* Maxwell *v.* Gibbs, 32 Iowa, 32 (1871), where plaintiff let a horse to an ostensible firm, and the holding-out partner was considered liable for the firm's injury of the animal.

[2] Stables *v.* Eley, 1 C. & P. 614 (1825), Abbott, C. J.

[3] Sir Frederick Pollock first pointed out this blunder. Lindley on Part. (5th ed.), *47, note *s*. See also Smith *v.* Bailey (1891), 2 Q. B. 403; 60 L. J. Q. B. 779.

[4] Taylor *v.* Wilson, 58 N. H. 465 (1878); Burdick's Cases on Part. 112.

[5] Green, Huffaker, & Co. *v.* Taylor & Son, 98 Ky. 330; 32 S. W. 945 (1895); Burdick's Cases on Part. 113.

(*a*) *Contests between Business and Individual Creditors.* — While the holding-out partner may be estopped from setting up his individual ownership as against creditors who have acted upon the faith of his representations that the title was in the firm, the estoppel is personal to him and should not affect his separate creditors,[1] in the absence of statutory provisions.

The weight of authority is in favor of this view,[2] although a different doctrine obtains in some jurisdictions. An elaborate discussion of the question will be found in the prevailing and the dissenting opinions in a recent Wisconsin case.[3] According to the majority of the court, it is "too clear for argument" that, "when there is an ostensible firm, by holding out to creditors generally the property of such firm ought to be considered, in equity, joint property for the administration thereof, in insolvency, the same as if such property belonged to a firm in fact"; and "such," it is asserted by the majority, "is the law as substantially declared by the Court of Appeals in Chancery of England."

The English decisions referred to, however, do not establish any such broad doctrine. They are based on a statutory provision that the property of a bankrupt divisible amongst his creditors shall include "all goods being, at the commencement of the bankruptcy, in the possession, order, or disposition of the bankrupt, in his trade or business, by the consent and permission of the true owner, under such circumstances that he is the reputed owner thereof."[4]

[1] Taylor *v.* Wilson, *supra.*

[2] Bixler *v.* Kresge, 169 Pa. St. 405; 32 At. 414 (1895); Broadway Nat. Bank *v.* Wood, 165 Mass. 312; 43 N. E. 100 (1896); Burdick's Cases on Part. 115, 129.

[3] Thayer *v.* Humphrey, 91 Wis. 276; 64 N. W. 1007 (1895); Burdick's Cases on Part. 117.

[4] 46 & 47 Vict. c. 52, § 44 (Bankruptcy Act of 1883).

It is true that the Lord Chancellor, in In re Rowland & Cranshaw,[1] observed that "the question of reputed ownership has nothing to do with the case," but in Ex parte Hayman,[2] the learned judges expressly declared that the right of the creditors of an ostensible firm to have the property, which is in the reputed ownership of such firm, treated as the joint estate of the firm, and not as the separate estate of its true owner, rests upon the statutory provision above referred to, and not upon the principles of equitable estoppel.

7. No Quasi Partnerships. — According to the view of the Wisconsin court, not only are persons who hold themselves out as members of a firm properly called *quasi* partners, but the ostensible firm is to be viewed as a *quasi* partnership. It is true that an eminent English writer has given currency to the term *quasi* partnership; but in his treatise it represents a different conception from that which is entertained by the Wisconsin and New York courts. It is employed by him for the purpose of showing an "ambiguity in the word *partnership* as used by English lawyers. Partnerships," he points out, "are by them divided into partnerships (properly so called), and partnerships as regards third persons, which are not in fact partnerships at all, and should never be so styled. What is called a partnership as regards third persons (*quasi* partnership) is nothing more than a number of persons who, in consequence of certain acts done by them, are held liable for each other's conduct, as if they had entered into a contract of partnership amongst themselves."

[1] L. R. 6 Ch. App. 421 (1866), Lord Cranworth, L. C.

[2] 8 Ch. Div. 11 (1878). See extracts from opinions of James and Thesiger, L. JJ., in Burdick's Cases on Part. 121. *Cf.* Lindley on Part. (5th ed.), *690. "The possession in this case was not in accordance with the title, whilst in Reynolds *v.* Bowley, L. R. 2 Q. B. 474 (case of a dormant partner) it was; and this seems to be the test in cases of this description."

*Quasi* partnership, as thus used by Lindley, refers only to the persons who hold themselves out as partners, and does not indicate that the property which is owned by these persons in severalty is to be treated by the courts as though it were the joint estate of a true partnership.

# CHAPTER III.

## THE NATURE OF A PARTNERSHIP.

### § 1. The Firm: Its Members: Its Name.

ONE of the most perplexing topics in partnership law is the nature of a firm. Undoubtedly the subject is inherently difficult; but its discussion has been rendered unusually troublesome by the multifarious and inconsistent doctrines which abound in judicial decisions. Perhaps the various conceptions of a partnership may be brought within one of the three classes now to be considered.

1. THE FIRM AS AN ASSOCIATION OF PERSONS. — Although occasionally an English judge has suggested "the notion of the existence of the firm as a separate entity from the existence of the partners," [1] the English bench and bar have maintained the view that "there is no such thing as a firm known to the law"; [2] that a firm has no separate existence as distinguished from the individual members, and does not partake of the nature of a corporation.[3] This view has received the approval of Parliament,[4] and is now

[1] Jessel, M. R., in Pooley *v.* Driver, 5 Ch. Div. 458 (1876).

[2] Ex parte Corbett, In re Shand, 14 Ch. D. 122 (1880); Burdick's Cases on Part. 134.

[3] Kay, L. J., In re Beauchamp Bros. (1894), 1 Q. B. 1, 7; Burdick's Cases on Part. 156, *n.*

[4] Partnership Act, 1890, § 4. (1) "Persons who have entered into partnership with one another are, for the purposes of this Act, called collectively a firm, and the name under which their business is carried on is called the firm name. (2) In Scotland a firm is a legal person distinct from the partners of whom it is composed, but an individual partner may be charged on a decree of diligence directed against

an established doctrine of English jurisprudence. It prevails also in most of the jurisdictions of this country. In the language of a learned judge, "A partnership cannot be considered as a person, in contradistinction to the persons composing it, simply because such is not its nature."[1]

2. THE FIRM AS AN ENTITY. — While English law "knows nothing of the firm as a body or artificial person distinct from the members composing it,"[2] the British Partnership Act[3] recognizes it in Scotland as "a legal person distinct from the partners of whom it is composed." In that country, "not only can it sue and be sued in 'the social name,' but it may sue and be sued by its own members."[4]

Similar doctrines obtain in some of our States. In Louisiana, whose jurisprudence is founded on the civil law, we should expect to find the firm spoken of as "the ideal being known as the partnership";[5] but in not a few of our common law States the courts have declared that "A partnership is a distinct entity, having its own property, debts, and credits. For the purposes for which it was

the firm, and on payment of the debts is entitled to relief *pro rata* from the firm and its members."

[1] Stayton, C. J., in Wiggins *v.* Blackshear, 86 Tex. 670; 26 S. W. 929 (1894); Burdick's Cases on Part. 198. In Bank of Buffalo *v.* Thompson, 121 N. Y. 280 (1890), Earl, J. said, "The firm is not recognized by lawyers as distinct from the members composing it"; and in Hallowell *v.* Blackstone Nat. Bank, 154 Mass. 359 (1891), Holmes, J. said: "Corey on Accounts and Lindley on Partnership have made it popular to refer to a mercantile distinction between the firm and its members. But we have no doubt that our merchants are perfectly aware that claims against their firms are claims against them." Burdick's Cases on Part. 286, 288.

[2] Pollock on Part. (5th ed.), 20.

[3] Quoted in a former note.

[4] Pollock on Part. (5th ed.), 21.

[5] Sherwood *v.* His Creditors, 42 La. Ann. 103 (1890); Burdick's Cases on Part. 678, 680.

created, it is a person, and as such is recognized by the law."[1] These judicial declarations are supported, to some extent, by statutory provisions authorizing actions to be brought by or against a partnership in its firm name, imposing taxes upon it, referring to it as an absconding or non-resident debtor, and the like.[2]

(*a*) *One Firm as Two Entities.* — In a few instances judges have treated a single firm, not as composed of natural persons, but as constituting two separate artificial persons. Taylor and Cassily were a firm having business houses in Cincinnati and New Orleans, Taylor living in New Orleans and Cassily in Cincinnati. A draft drawn in Cincinnati, by a creditor of the firm, on "Taylor and Cassily, New Orleans," and accepted in Cincinnati by Cassily, was held to be drawn on a mercantile "person without the jurisdiction of" Ohio. The branch house in New Orleans was treated as an ideal person, domiciled there, and the bill it was said was drawn, not on the natural persons Taylor and Cassily, but on the New Orleans house.[3] And yet there can be no doubt that the holder of the bill might have maintained an action thereupon against Taylor and Cassily as individuals in Ohio, and might have enforced his judgment against the property of the Cincinnati house.[4] Moreover, had the members of the firm been sued in a State court of Ohio, they could not have secured a removal of the cause to a Federal court on the ground that the firm was a resident of Louisiana.[5]

[1] Richards *v.* Le Veille, 44 Neb. 38; 62 N. W. 304 (1895); Burdick's Cases on Part. 281, 282; *cf.* Teague *v.* Lindsey, 106 Ala. 266; 17 So. 538 (1895); Burdick's Cases on Part. 207, *n.*

[2] Drucher *v.* Wellhouse, 82 Ga. 129 (1888); Burdick's Cases on Part. 131.

[3] West *v.* The Valley Bank, 6 Ohio St. 168 (1856); Burdick's Cases on Part. 132.

[4] Wright *v.* Hooker, 10 N. Y. 51 (1854).

[5] Adams *v.* May, 27 Fed. 907 (1886).

Equally untenable with this Ohio decision is the dictum of a distinguished New York judge, that a bill drawn by Page & Co. on White & Co., and accepted by the drawees, had upon it the names of two firms; it appearing that Page, Barnard, and White as partners carried on business at Oswego, N.Y., in the name of Page & Co., and at Albany in the name of White & Co.[1] Here was but a single business entity.

(b) *Not treated as Two Entities in Bankruptcy.* — The intimation of the learned judge that, had the partners gone into bankruptcy, the house of Page & Co. would have been treated as entirely distinct from that of White & Co., and that the assets of each would have been first distributable to its creditors is not borne out by the authorities cited in its support.[2] In the first of the two cases which were referred to, Nims and Long had been partners under the name of O. L. Nims & Co. They dissolved, and Long formed a partnership with Evans. After the dissolution of this firm Nims and Long entered into a new partnership under the name of O. L. Nims, Agt. Upon the bankruptcy of Nims and Long, it was properly held that the debts of O. L. Nims & Co. were not provable against the assets of the firm of O. L. Nims, Agt. The second citation is not of a case where the same partnership carried on business in two names. The question in Forsyth *v.* Woods was whether a joint contract of the partners made in their individual names respecting a matter that had no connection with the firm business created a liability of the firm as such. Justice Strong declared that it did not. The opinion does not contain an intimation in favor of Judge Ruger's dictum.

But where the same partnership carries on business

[1] Second Nat. Bank *v.* Burt, 93 N. Y. 233 (1883).

[2] In re Nims, 16 Blatch. 439 (1879), and Forsyth *v.* Woods, 11 Wall. (U. S.) 484 (1870).

in different places, the assets of the various houses constitute but a single joint fund, and there is but one set of firm creditors, although the business in one place may not be of the same character as that in the other places, and although the different branches may have different names as well as keep distinct accounts.[1]

3. PARTNERSHIP AS A STATUS. — Still a third view of the nature of a firm has been propounded by a learned and ingenious writer. According to his conception, partnership is a status. In his own language:[2] "The sum of the rights and duties of the partners in the relation is called the status of partnership. The status may be created by contract, like marriage or sale. The contract is the occasion or door, and the consummation or conveyance establishes rights *in rem.*" "Though partnership may be dissolved at will, and the relation brought to a close through the act of the individual, yet the status, with all its attendant duties and prerogatives, subsists until it is terminated in a manner consistent with its original purpose." "The elevation of partnership into a status is due to the presence of a firm estate." "The partners, being merged as individuals in the firm estate, are enabled to trade in a distinct capacity." "The only qualification is, that in acting as partners they bind their separate estates, and the firm creditor is not confined to the firm fund." "It is the recognition by the law of the estate that severs the partner from himself as a man."

This learned author has no tolerance for the fiction that the firm is a person, which "contracts debts, and charges its assets for payment. If the fiction had a legal basis for its existence," he declares, "and was consistently carried out, a partnership would become a corporation." Refer-

[1] Campbell *v.* Colorado Coal & Iron Co., 9 Col. 60; 10 Pac. 248 (1885); Banco de Portugal *v.* Waddel, 5 App. Cas. 161 (1881).

[2] Parsons (James), Principles of Part. (1st ed.), 696, 290, 291.

ring to a distinguished advocate of this fiction, he asks, "What is the polarity of mind of a lawyer who advocates making a partnership by turns a corporation and a number of individuals? (The Law of Partnership, Ch. X. § 1, by Theophilus Parsons, LL.D.)"; and adds, "If he comprehended the elemental distinction of kind, he would not expose his confusion by making the suggestion, but he would disguise the proposition in the jargon of lawyers, who speak of a man *quo modo* a horse."[1]

4. THE MERITS OF THESE VIEWS. — No attempt will be made at present to estimate the comparative merits of these various conceptions of a partnership. Each view will be discussed in connection with the authorities which support or antagonize it. Meanwhile we pass to the consideration of topics upon which there is substantial unanimity of opinion.

5. FIRM NAME IS A NON-ESSENTIAL. — A partnership may exist without a firm name,[2] although one is usually agreed upon by the parties; and the absence of a stipulation on this point is indicative of their intention not to form the partnership relation.[3] If a firm name has not been agreed upon, either partner may adopt one, and the fact that he has employed a particular name in one transaction does not preclude him from using a different style on another occasion.[4]

In the absence of any statutory provision[5] or settled

[1] Parsons (James), Principles of Part. (1st ed.), 286, 287.

[2] Le Roy *v.* Johnson, 2 Pet. 186 (1829); Stickney *v.* Smith, 5 Minn. 486 (1861).

[3] Farrand *v.* Gleason, 56 Vt. 633 (1884); Burdick's Cases on Part. 27.

[4] McGregor *v.* Cleveland, 5 Wend. (N. Y.) 475 (1830).

[5] The New York Court of Appeals has characterized a statute which prohibits the use of "and Company," or "& Co.," unless it shall represent an actual partner, as well as the use of the name of a person not interested in the firm, as "not a very useful statute." Gay

doctrine of public policy to the contrary, the firm style need not contain the name of any of the partners;[1] it may be fanciful or may purport to be that of a corporation.[2] In some States, the assumption of a corporate name in any sign or advertisement, for the purpose of soliciting business, by an unincorporated association, is punishable by a fine.[3]

(*a*) *Limitation on Liberty of Choice.* — The right to select any appellation as a firm name has this important limitation: it must not be exercised in such a way as to work a fraud upon others trading under substantially the same name, or upon the public. No person or body of persons can obtain an exclusive right to a name at common law. Accordingly, persons trading as "Rogers & Bro.," cannot lawfully complain because others trade in the name of "C. Rogers & Bros.," if this is done in an honest and ordinary business manner.[4] "Where the only confusion created is that which results from the similarity of the names, the courts will not interfere. A person cannot make a trade mark of his own name, and thus obtain a monopoly of it which will debar all other persons of the same name from using their own names in their own business."[5]

*v.* Siebold, 97 N. Y. 472 (1884). Other decisions bearing on this statute (L. 1833, ch. 281, now Pen. Code, § 363) are Zimmerman *v.* Erhard, 83 N. Y. 74 (1880); Wood *v.* Railway Co., 72 N. Y. 196 (1878).

[1] Bank of Rochester *v.* Monteath, 1 Den. (N. Y.) 402 (1845). Keeler, Allen, and Geo. Monteath did business in the name of Wm. Monteath, who acted as their agent.

[2] Holbrook *v.* Ins. Co., 25 Minn. 229 (1878). "It is said to be an offence against the prerogative of the Crown for private persons to 'assume to act as a corporation.' But it is by no means clear how it can be punished, though possibly the Queen's Bench Division may have the jurisdiction to punish it by fine." Pollock's Digest of Part. (5th ed.), 22.

[3] Illinois Crim. Code, § 220.

[4] Rogers *v.* Rogers, 53 Conn. 121; 55 Am. R. 78 (1885).

[5] Meneely *v.* Meneely, 62 N. Y. 427 (1875). The name of plaintiffs'

But if a trader or firm has carried on a business under a particular name, such as the "Guinea Coal Company," it is a fraud upon such trader or firm, as well as upon the public, for another trader or firm to set up a rival business "in such a way as to induce persons to deal with him or them in the belief that they are dealing with the trader or firm who gave a reputation to the name."[1]

(*b*) *Firm Name is the Name of each Member.* — Upon this point common law authorities are in accord, wholly ignoring the idea of the firm as an entity distinct from its members. The authorized signature of the partnership name operates as the signature of each partner.[2] If the firm name is "D'Este & Co.," a note having that signature is properly described as a note made by the partners composing the firm.[3] If Lewis, Gorthwaite, and Grant are trading in New York under the name of Lewis, Gorthwaite, & Co., and in New Orleans under the name of Grant,

firm was E. A. & G. R. Meneely; that of defendants' was Meneely & Kimberly. Plaintiffs had stamped their goods "Meneely's, West Troy, N. Y." Defendants stamped theirs "Meneely & Kimberly, Troy, N. Y." The court did not interfere.

[1] Lee *v.* Haley, 5 Ch. App. 155 (1869). The rival business was conducted in the name of "Pall Mall Guinea Coal Company," and defendant's envelopes and business cards were printed in such a way as to resemble the plaintiff's.

"The rules governing the use of firm or trade names obviously belong, properly speaking, not to the law of partnership, but to that subdivision of the general law of ownership which has to do with copyright and other analogous rights." Pollock's Digest of Part. (5th ed.), 21.

[2] This is sometimes changed by statute. See Swift *v.* Jewsbury, L. R. 9 Q. B. 301 (1874), under 8 & 9 Geo. IV. c. 14, § 6, providing that one shall not be liable for a false representation as to the solvency of another, unless it is in writing, and signed by him; no provision being made for signing by an agent.

[3] Haskins *v.* D'Este, 133 Mass. 356 (1882); Burdick's Cases on Part. 135.

Lewis, & Co., notes payable to Lewis, Gorthwaite, & Co. may be joined in an action with those payable to Grant, Lewis, & Co., and all may be described as payable to Lewis, Gorthwaite, and Grant.[1]

At common law a man may change his name at pleasure,[2] and may make contracts under any name he may choose to assume, even though it may be a fictitious name.[3] Accordingly, where a firm did business in the name of the "Royal Flint Glass Works," a warrant of attorney to confess judgment, which was executed in that name by the president and treasurer of the firm, with the assent of the various partners, was held to be the warrant of each partner.[4]

On the other hand, the firm name represents only those who are partners when it is employed. Hence, "if a legacy is left to a firm, it is payable to those who compose the firm at the time the legacy vests."[5]

(*c*) *Individual Signatures equivalent to Firm Name.* — Whether the partners have agreed upon a name for their firm or not, its employment is not necessary to the validity of a firm contract. Notes signed with the individual names of the partners,[6] or with the name of but one of them,[7] will bind the firm if they were issued as firm contracts. Treating such "notes as firm obligations would not be in-

[1] Messner *v.* Lewis, 20 Tex. 221 (1857); Burdick's Cases on Part. 133.

[2] Petition of Snook, 2 Hilt. 566 (1859).

[3] Shain *v.* Du Jardin, 38 Pac. (Cal.) 529 (1894); Burdick's Cases on Part. 138, *n.*

[4] Miller *v.* Royal Flint Glass Works, 172 Pa. St. 70; 33 At. 350 (1895); Burdick's Cases on Part. 137.

[5] Stubbs *v.* Sargon, 2 Keen, 255 (1837). See other applications of this principle in Lindley on Part. (5th ed.), *113, 114.

[6] Dreyfus *v.* Union Nat. Bank, 164 Ill. 83; 45 N. E. 408 (1896); Burdick's Cases on Part. 139.

[7] Sage *v.* Sherman, 2 N. Y. 417 (1849).

consistent with their face. To determine the fact whether they are such, it is necessary to inquire into the nature of the transaction out of which they grew, and how it was intended they should operate."[1]

As the firm name is but a conventional appellation for its various members, firm and individual names may be interchanged at pleasure. If J. S. Allen and H. H. Hayes are partners under the style of Allen and Hayes, a note payable to them in their individual names is validly indorsed in the name of Allen and Hayes.[2]

(*d*) *Assent necessary to a Valid Change of Firm Name.* — It is to be borne in mind, in this connection, that when the partners have agreed upon a firm name, it cannot be changed without their consent. Consequently, if negotiable paper is issued by a partner in other than the stipulated firm name, it will not be binding on the partners who did not authorize the signature, or have not ratified it, unless the variation is immaterial.[3] The principles underlying the cases in the preceding note will be discussed in the next chapter.

(*e*) *Name of one Partner as a Firm Name.* — If the partners assent to the adoption of the individual name of

[1] Dreyfus *v.* Union Nat. Bank, *supra.* In this case the notes were given in partial payment of the purchase price of lands, which the evidence showed was bought for the firm, paid for in part with firm moneys, and entered on the firm's books as partnership assets; hence the notes were held to be a proper charge against the assets of the firm in the hands of an assignee for the benefit of creditors. *Cf.* Berkshire Woolen Co. *v.* Guillard, 75 N. Y. 535 (1879); where a joint obligation under seal, executed by all the members of a firm in its business and for its benefit, was held to be a partnership obligation.

[2] Mick *v.* Howard, 1 Ind. 250 (1848); Burdick's Cases on Part. 131.

[3] Palmer *v.* Stevens, 1 Den. (N. Y.) 471 (1845); Williamson *v.* Johnson, 1 B. & C. 146 (1823); Faith *v.* Richmond, 11 A. & E. 339 (1840); Tilford *v.* Ramsay, 37 Mo. 563. *Cf.* Lindley on Part. (5th ed.). *185, 186.

one of their number as their firm name, contracts executed in that style for the partnership will be enforceable against all.[1] In case the individual member "carries on no business separate from that of the firm, there is a presumption that a bill of exchange, drawn, accepted, or indorsed in the common name, is a bill drawn, accepted, or indorsed for the partnership, and for which the partnership is liable."[2] This presumption is based upon considerations of business convenience and expediency. "The vast majority of the bills," said the court in the last cited case, "given under the circumstances supposed, would be really partnership bills, and yet it would be often difficult, if not impossible, for the holders of such bills to do more than prove that the only trade carried on under the individual name was the trade of the partnership; and if they were compelled to go further, and prove that the particular bill was a partnership bill, the effect might be that in many cases dormant partners, and in some cases ostensible ones too, might escape from just liability."

If the partner in whose name the firm trades carries on a separate business, there is no basis for the presumption stated above. The signature of this name, common to the firm and to the individual trader, "may be on his own individual account, as his personal contract, or it may be on account of the partnership. Upon the face of the paper it stands indifferent. The burden of proof is upon the plaintiffs to establish that it is a contract of the firm, and ought to bind them."[3]

(*f*) *Cases rarely decided on the Presumption alone.*— While it is important to bear in mind this presumption, the observation of the learned judge in Yorkshire Banking

[1] Bank of South Car. *v.* Case, 8 B. & C. 427 (1828).

[2] Yorkshire Banking Co. *v.* Beatson, 5 C. P. D. 109: 42 L. T. N. S. 455 (1880); Burdick's Cases on Part. 141.

[3] U. S. Bank *v.* Binney, 5 Mason (U. S.) 176 (1828).

Co. *v.* Beatson[1] should be remembered, that "there are likely to be few, if any, cases where the decision of the jury or of a court will be rested upon the presumption alone." In that case, Beatson carried on no separate business, and the jury found that the plaintiff took the bills in suit as the bills of the chemical works (the partnership business of Beatson and Wycock), whoever the proprietors might be, yet the court held that the presumption in favor of plaintiff was overborne by the additional facts that the bills were in truth private transactions of Beatson, not intended to bind the firm nor enuring to its benefit. "Beatson," it was said, "by giving the use of his name to a partnership of which he was a member, and the only ostensible member, did not preclude himself from making contracts binding on himself alone, and in any contracts *de facto* made by him, whether by parol or in writing, the question, the answer to which would determine Wycock's liability or freedom from liability, would not be whether the other contracting party trusted Beatson because he supposed him to be the sole owner of the chemical works, but whether Beatson, whom alone he knew and actually trusted, was acting as agent for the partnership, or in his individual capacity for himself."[2]

6. Suits by and against a Partnership. — We have

[1] 5 C. P. D. 109 (1880); Burdick's Cases on Part. 141.

[2] Fosdick *v.* Van Horn, 40 Ohio St. 459 (1884), *accord.* In this case it is said: "If suit is brought on a promissory note for borrowed money, bearing the signature of the common firm name, the presumption is that it is the note of the firm not containing the dormant partner. The plaintiff, to recover against the dormant partner, must prove either that the consideration of the note was obtained on the credit of the firm in which the dormant partner was interested, or that it enured to the benefit of that firm. That it was upon the credit of that firm that the money was borrowed may be proved by the declarations to that effect of the ostensible partners at the time of the loan, or it may be proved by circumstances."

seen that a partnership cannot sue or be sued as an artificial person, at common law, but that suits must be brought by or against its members. And yet the peculiar relation of the partners does affect the rights of third persons in such suits.

For example, if the members of a firm are sued as partners for damages sustained by the plaintiff, while in their employment, it is error to receive an admission made by one of the defendants after the accident from which negligence could be inferred, even though the court instructs the jury that its effect is to be limited to the partner who made the statement.

In dealing with this question, the Supreme Court of Pennsylvania declared, "As the action was against the firm, there could practically be no such limitation";[1] for the action as well as the judgment was joint, and process to enforce the judgment could be levied on the firm assets. Of course, admissions made by one partner in such circumstances as to be binding upon the firm are receivable in actions against the partnership; but in such cases they are the admissions of the firm, and not those of the individual partner only.

Although the case just cited suggests the conception of a partnership as an entity, that conception is modified by other cases, one of which is now to be considered. The surviving members, having sued for legal services rendered by the firm, were met by the objections that the firm was a legal person which had died upon the death of one of its members, and that a dead person cannot sue. "But," said the court, "a firm is not a person in the sense supposed. For technical purposes of suing and being sued, the law does not know the firm, but only the men composing it. If we leave technicalities on one side, and consider

[1] Folk v. Schaeffer, 180 Pa. St. 613; 37 At. 104 (1897); Burdick's Cases on Part. 158.

practical convenience, it would not do at all to let dissolution — for instance, by the death of a member — prevent the collection of debts due to the firm." [1]

7. FIRMS WHICH INCLUDE INFANT PARTNERS. — Perhaps the cases which afford the greatest support to the conception of a firm as an entity are those in which the rights and liabilities attaching to partnerships containing infant members have been adjudicated. It is true the doctrine has not been formally declared in these decisions, but it is difficult to uphold them upon any other theory.

Undoubtedly an infant who without fraud enters into partnership with an adult can hold the latter to this contract, as to any other business agreement. He can exercise the powers of a partner, buy and sell its goods, and subject it to contract and tort liabilities. On the other hand, he has the legal right, during infancy [2] or at maturity, to repudiate his contract of partnership, as well as his responsibility for firm obligations. In case he exercises this right, two important questions arise: First, How does it affect the rights of firm creditors? Second, How does it affect the adult partner?

(*a*) *The Rights of Firm Creditors after Repudiation by an Infant Partner.* — In case the repudiation is confined to the infant's liability for firm obligations, it is well settled that his plea of infancy will not affect the rights of firm creditors against the firm assets. Accordingly, if actions against the firm are instituted by various creditors, and the minor partner sets up the defence of infancy against some of the plaintiffs while he does not against others, all of the judgments are enforceable against the

[1] Hyde *v.* Moxie Nerve Food Co., 160 Mass. 559; 36 N. E. 585 (1894); Burdick's Cases on Part. 159.

[2] In Dutton *v.* Brown, 31 Mich. 182 (1875), it was declared that an infant could not disaffirm his contract of partnership during minority; but this is not the general view. Lindley on Part. (5th ed.), *75.

firm assets, although some of them are entered against the adult partner only. Such a defence leaves the partnership contract still in force, and gives to the adult partner the right to have the firm property applied to the firm debts, and to have "each partner contribute his *pro rata* share to the payment of any partnership indebtedness remaining after applying the partnership property."[1]

There seems to be no doubt that the courts will accord the same rights to firm creditors, even though the infant repudiate the partnership contract, and thus relieve himself from personal liability to firm creditors, as well as from liability to the adult partner for contribution. The Supreme Court of New Hampshire[2] has declared: "If an infant partner can repudiate his contract of partnership and call for a return of his share in the capital, without regard to the account of profit and loss, it must he upon some proceeding instituted for that purpose and in which the rights of the other partners and of the creditors may be considered and protected."

A similar view is presented in an opinion of the New York Court of Appeals: "It cannot be doubted but that the law would devote the assets of the firm to the discharge of the partnership obligations, whenever any court should be appealed to for that purpose. . . . It is not too much to say that, if an infant goes into a mercantile adventure which proves unsuccessful, he ought at least to be held so far as that the assets acquired by the firm should be applied to the payment of the debts of the concern."[3]

Such, too, is the doctrine of the House of Lords. "The adult partner is, however, entitled to insist that the partnership assets shall be applied in payment of the liabil-

1 Whittemore *v.* Elliott, 7 Hun (N. Y.) 518 (1876).

2 Gay *v.* Johnson, 32 N. H. 167 (1855).

3 Yates *v.* Lyon, 61 N. Y. 344 (1875).

ities of the partnership, and that until these are provided for no part of them shall be received by the infant partner. And if the proper steps are taken, this right of the adult partner can be made available for the benefit of the creditors."[1]

(*b*) *Bankruptcy of a Firm with an Infant Member.* — In Britain an infant "cannot be made subject to the bankrupt laws in respect of any debt contracted by a firm of which he is a partner"; but his infancy will not prevent an adjudication of bankruptcy against the firm. This question, which proved to be a perplexing one to the English courts, was settled by the House of Lords in the case last referred to. Firm creditors brought an action against the firm in the firm name of Beauchamp Brothers, pursuant to a provision of the rules of court. Gilbert W. Beauchamp, the infant partner, appeared by his guardian *ad litem* and objected that he was not liable. A variety of views was presented by the judges of the lower courts as to the proper form of judgment in such a case, and the proper form of proceedings in bankruptcy, upon the failure of the firm to pay the judgment. In the House of Lords it was ruled that the judgment should have been either against Ralph Beauchamp, the adult partner, or against the firm other than Gilbert W. Beauchamp; and that the bankruptcy proceeding should have been against the firm of Beauchamp Brothers other than Gilbert W. Beauchamp. It was also ruled that in the bankruptcy proceedings the partnership assets were available for firm creditors. These rulings, it is submitted, are a virtual recognition of the firm as an entity distinct from its members.[2]

1 Lovell & Christmas *v.* Beauchamp (1894), Appeal Cas. 607; Burdick's Cases on Part. 155.

2 "These rules, it will be observed, do not introduce anything that amounts to the recognition of the firm as an artificial person distinct from its members." Pollock on Part. (5th ed., 1890), 131, citing from

(*c*) *The Firm acquires Title to the Infant's Contribution.* — While this doctrine has not been formally declared by the courts, it appears to be sustained by the cases already cited. If the firm does not obtain a title of its own to the contributions of its members, it is difficult to understand why an infant partner cannot "reclaim his share of the firm property at any time on his title as cotenant, irrespective of the state of account between himself and his copartners," to the exclusion of the claims of firm creditors against the firm fund.[1] And yet, as we have seen, the courts have uniformly denied this right to the infant.

Undoubtedly, if the infant has been induced to enter the partnership by false representations of the adult member, he can maintain an action against the adult for the

James, L. J., in Ex parte Blain, 12 Ch. D., at p. 533 (1879), the following sentence: "We have not yet introduced into our law the notion that a firm is a *persona*."

[1] "Suppose the infant partner upon majority repudiated the partnership, and reclaimed his contribution of $10,000, and the only assets of the firm were goods of that value, sold in one lot by a vendor, who claimed payment of the price. Is the infant preferred to the unpaid seller, and allowed to take the assets away from him without payment? The infant would take the merchandise from his copartner, who could not resist his demand. The creditor could not prevent it. He sold to the infant and adult partners, but could recover only from the adult. The infant's taking the goods would not be a retention which would charge him for the price, because he would not take them under his contract with the seller, but under his contract with his copartner, which he might avoid at age. The goods became the property of the partners by virtue of the sale, and, thus converted into firm assets, lost their identity. The infant reclaims them as representing his contribution." "The firm does not acquire by virtue of the contract of partnership a joint title, so as to subject the infant's contribution or interest in the firm fund to the claims of firm creditors. The interest of the infant is always that of a tenant in common, because he is not liable to an account." Parsons's (James) Principles of Part. (1st ed.), §§ 136, 137.

rescission of the contract and the recovery of his contribution, less any sum received by him from the business, where the rights of firm creditors are not involved.[1] But in the absence of fraud, an action to recover his contribution cannot be maintained by the infant;[2] nor can he recover the premium paid for admission to a firm.[3]

(*d*) *Rights of the Adult against the Infant Partner.* — While a contract of partnership between an adult and a minor is ordinarily binding upon the former, yet if it has been induced by the minor's fraud, a court of equity will rescind it at the suit of the adult;[4] and in case of the minor's misconduct the partnership may be dissolved.[5] Infancy will shield the minor from liability for firm debts, from his obligation to perform the duties of a partner or to observe the terms of the partnership agreement, and even from the costs of a suit for dissolution, but he will not be permitted to use it as a weapon for his partner's undoing.

### § 2. Firm Title: How Taken and Held.

The title to chattels which are acquired by a partnership in ordinary business transactions vests in the firm, whatever may be its name or style. Nor will it matter that the transfer of such property is evidenced by a contract under seal.[6] In the case of real property, however, a different doctrine prevails, generally to the effect that a deed of conveyance to a firm by its firm name does not vest the legal title in the firm.

[1] Sparman *v.* Keim, 83 N. Y. 245 (1880).

[2] Page *v.* Morse, 128 Mass. 99 (1880).

[3] Adams *v.* Beall, 67 Md. 53; 1 Am. St. R. 379 (1887).

[4] Lempriere *v.* Lange, 12 Ch. D. 675 (1879). This was a case of lease, but the principle announced warrants the statement in the text.

[5] Bush *v.* Linthicum, 59 Md. 344 (1882); Burdick's Cases on Part. 154.

[6] Hendren *v.* Wing, 60 Ark. 561; 31 S. W. 149 (1895); Burdick's Cases on Part. 161.

1. Name of Grantee must be that of a Natural Person. — This rests upon a perversion of the common law rule, that it is necessary in a grant that the grantees should be named, otherwise the grant can in law have no operation. If the name adopted as a firm style does not include the name of a natural person, a deed to the firm in such name, it is said, passes nothing at law; it has no more legal effect than a deed in which the name of the grantee is that of a dead person. If the name includes the name of a natural person, for example, J. M. Whitehill & Co., a deed to the firm name conveys the legal title to the natural person, J. M. Whitehill;[1] and such person can convey a perfect legal title to a grantee of the firm.[2]

(*a*) *Firm may be the Grantee.* — In England, and in some of our States, the common law rule has not been thus perverted; and a deed of land to a firm in its business name conveys the legal title to the property to those who use that "style and firm."[3] This is quite in accord with the early common law conception of a deed, as stated in Sheppard's Touchstone, at p. 236: "If the grant do not intend to describe the grantee by his own name, but by some other matter, then it may be good by a certain description of the person, without either surname or name of baptism. *Id certum est quod certum reddi potest.*"

In order to avoid any difficulty, however, a deed to a firm should contain the names of the various partners as well as the name in which they are carrying on business.[4]

[1] Riddle *v.* Whitehill, 135 U. S. 621; 10 Sup. Ct. 924 (1889).

[2] Woodward *v.* McAdam, 101 Cal. 438; 35 Pac. 1016 (1894); Burdick's Cases on Part. 163.

[3] Maugham *v.* Sharpe, 17 C. B. N. S. 443 (1864); Burdick's Cases on Part. 160; Hoffman *v.* Porter, 2 Brock. (U. S. C. C.) 158 (1824); Jones *v.* Neale, 2 Pat. & H. (Va.) 339 (1856); Brunson *v.* Morgan, 76 Ala. 593 (1884).

[4] Lauffer *v.* Cavett, 87 Pa. St. 479 (1878). In Davis *v.* Davis, 60 Miss. 615 (1882), Burdick's Cases on Part. 164 *n.*, however, it was

2. EQUITY RECOGNIZES OWNERSHIP IN THE FIRM. — Although the legal title may be vested by a conveyance in one partner, or may be vested in several members as tenants in common, equity will compel the possessor of such title to hold and to transfer it for the firm's benefit. It treats such possessor as a trustee for the firm.[1] In the language of an eminent judge:[2] "In the view of equity it is immaterial in whose name the legal title of the property stands, — whether in the individual name of a copartner or in the joint names of all; it is first subject to the payment of the partnership debts, and is then to be distributed among the copartners according to their respective rights. The possessor of the legal title in such case holds the property in trust for the purposes of the copartnership."

(*a*) *Purchaser from Holder of Legal Title.* — In such cases, however, the interest of the firm in the property is only an equitable one. Having permitted the legal title to stand in the name of one of its members, neither the firm nor its creditors can enforce the equitable interest against a *bona fide* purchaser for value from the legal owner.[3] But a purchaser with notice, although for value, will take the property subject to the firm's equitable claim.[4]

said that the deed should run to H. L. Davis & Co., so as to show that the purchase was made by partners for firm purposes and not by co-tenants.

[1] Delmonico *v.* Guillaume, 2 Sand. Ch. 366 (1845); Burdick's Cases on Part. 161.

[2] Field, C. J., in Dupuy *v.* Leavenworth, 17 Cal. 262 (1861).

[3] Robinson Bank *v.* Miller, 153 Ill. 244; 38 N. E. 1078 (1894); Burdick's Cases on Part. 165. In this case, land was bought by three men as tenants in common, who formed a partnership later and used the land in the firm business. Although it was milling property, and was used by them as partners in the milling and grain business, the court held that these facts were not necessarily notice of a partnership in the land.

[4] Mattock *v.* James, 13 N. J. Eq. 126 (1860).

The separate creditors of the individual member holding the legal title are not purchasers for value,[1] and judgments obtained by them do not affect the equitable interest of the firm, nor give them a preference over firm creditors.[2]

(*b*) *Firm Creditors may follow Proceeds.* — In case the partner who holds the legal title disposes of the property to a *bona fide* purchaser, and invests the proceeds in other property, equity will enable the firm or its creditors to take the property so acquired in lieu of the partnership property.[3]

3. Partners are not Tenants in Common. — The real property of a firm is not held by its members as tenants in common. If it were, any partner might maintain an action for its partition upon the dissolution of the firm. But it is well settled that he has no such right, so long at least as the partnership affairs remain unadjusted. In England the right is absolutely denied. Upon dissolution, the partnership assets must be sold,[4] in the absence of an agreement of the partners to the contrary, although no firm debts are owing to outsiders; it is necessary "for the purpose of settling the rights between the partners."[5]

[1] Goldthwaite *v.* Janney, 102 Ala. 431; 15 So. 560 (1894); Burdick's Cases on Part. 176.

[2] Page *v.* Thomas, 43 Oh. St. 38; 1 N. E. 79 (1885). A different doctrine obtains in Pennsylvania, where it is held that "no partner has the right to contradict the legal title, after a lien has attached." Parsons (James), Principles of Partnership (1st ed.), § 111 and cases cited.

[3] Chalfant *v.* Grant, 3 Lea (Tenn.) 118 (1879).

[4] Partnership Act, 1890, § 39; Lindley on Part. (5th ed.), *555.

[5] Wild *v.* Milne, 26 Beav. 504 (1859); Burdick's Cases on Part. 166. In this case, the Master of Rolls referred to the singular inconveniences which would follow a decree for partition: "Would the steam engine be included in the division, and, if so, how could it be possible to make a partition of the remainder? Are all the parties to have the use of the shaft, or a right of descending by means of the machinery? The court is compelled, by the exigency and circumstances of these cases, to direct a sale."

In this country, an action for partition cannot be maintained so long as the property may be needed for the payment of firm debts. While these debts remain unsatisfied each partner has a right to insist that firm assets shall be applied to their liquidation. Out of this equity, it has been said, "has emerged the rule that the partition of the real property of a firm will not be decreed, so long as debts of the partnership remain unliquidated. . . . The only method by which a partner, under such conditions, can compel a division of the firm property is by a bill to administer and settle the partnership affairs."[1]

(*a*) *When Partition allowed in the United States.* — In the case last cited, the evidence disclosed that the only outstanding claim against the firm was in litigation in the courts of New York; that the firm owned real property in that State which was more than sufficient for the satisfaction of the claim; while the real estate sought to be partitioned was located in New Jersey, which was the State of the firm's domicile. The court decided that inasmuch as the ground for refusing partition is that partners may be protected from future calls to pay firm debts, it having been shown in this case that the property involved in the application for partition would not be needed to meet such obligations, all objection to such distribution disappeared.

(*b*) *Principle underlying the English View.* — This differs radically from that announced in the case last referred to, and has been stated as follows:[2] "On the dissolution of the partnership, all the property belonging to the partnership shall be sold, and the proceeds of the sale, after discharging all the partnership debts and liabilities, shall be divided among the partners, according to their respective shares in the capital. That is the general

[1] Molineaux *v.* Raynolds, 54 N. J. Eq. 559; 35 At. 536 (1896); Burdick's Cases on Part. 169.

[2] Darby *v.* Darby, 3 Drewry, 495 (1856).

rule; it requires no special stipulation; it is inherent in the very contract of partnership. . . . The mere contract of partnership, without any express stipulation, involves in it an implied contract, quite as stringent as if it were expressed, that, at the dissolution of the partnership, all the property then belonging to the partnership, whether it be ordinary stock in trade, or a leasehold interest, or a fee simple estate in land, shall be sold, and the net proceeds, after satisfying all the partnership debts and liabilities, be divided among the partners; and that each partner and the representatives of any deceased partner, have a right to insist on this being done."

(*c*) *Principle Criticised.* — The existence of this implied agreement has been denied in this country. "If the inference of such an agreement," a learned judge has said, "is to be made as part of the transaction of purchasing real estate with partnership funds for partnership use, it is equally inconsistent with the failure to express such a term in the deed of conveyance. The inconsistency is even greater than that; for by the express terms of the deed and by the well known operation of law, the estate is limited to the heirs of the several copartners, whose estate is at law the ordinary one of tenants in common."[1]

(*d*) *A Mischievous Heresy.* — This statement, that at law copartners are tenants in common, although constantly recurring in judicial opinions and in text books, is unsound and mischievous. That it is the source of needless confusion in partnership law will be clearly seen, when we examine the rights and remedies of creditors. Its inaccuracy will be fully disclosed in the next section. The New York Court of Appeals has denied the accuracy of the statement in explicit terms.[2] In the case referred to, William B. and Simeon Fitch, upon the dissolution of

[1] Shearer *v.* Shearer, 98 Mass. 107 (1867).

[2] Preston *v.* Fitch, 137 N. Y. 41; 33 N. E. 77 (1893).

their partnership agreed that they should continue to hold as tenants in common a certain debt due the firm. The debt was secured by mortgages and other liens. The former partners began a foreclosure of these mortgages. Upon the death of Simeon, William, as survivor, continued the foreclosure suit, and during its progress paid out considerable sums of money. Simeon's representatives denied their liability to contribute towards these disbursements, on the ground that their testator was a tenant in common with William, and that the latter's expenditures had not been requested by their testator nor by them. But the court declared that the intention of the parties was not to change the nature of their title, — "they described such holding as a tenancy in common, when in law it was a holding as partners." As their title was that of partners, and not of tenants in common, the court decided that William, as surviving partner, had the legal right to incur all proper and reasonable expenses in the foreclosure action, and that the estate of Simeon must contribute towards their reimbursement.

The unsoundness of the doctrine that the legal estate of partners is that of tenants in common, is also affirmed by the Supreme Court of Wisconsin.[1] The title to firm property had been taken in the name of one partner, with the assent of his copartner. The latter having brought an action to have the legal title vested in both partners as tenants in common, his complaint was dismissed, the court declaring that he "had no right to call for a conveyance of his interest as a tenant in common of the lots until the trust fastened upon them for partnership purposes had been fully satisfied. . . . The remedy of the plaintiff, if any, was only by action to dissolve the copartnership, and for an accounting and proper application of the assets."

[1] Kruschke *v.* Stefan, 83 Wis. 373; 53 N. W. 678 (1892); Burdick's Cases on Part. 167.

4. FIRM REAL ESTATE CONVERTED INTO PERSONALTY. — The modern English rule on this topic, as authoritatively stated in the Partnership Act of 1890, is as follows: "Where land or any heritable interest therein has become partnership property, it shall, unless the contrary intention appears, be treated as between the partners (including the representatives of a deceased partner), and also as between the heirs of a deceased partner and his executors or administrators, as personal or movable and not real or heritable estate." "Provided that the legal estate or interest in any land, or in Scotland the title to or interest in any heritable estate, which belongs to the partnership, shall devolve according to the nature and tenure thereof, and the general rules of law thereto applicable, but in trust, so far as necessary, for the persons beneficially interested in the land." [1]

This rule followed logically from the principle that a partner's share "is nothing more than his proportion of the partnership assets after they have been turned into money and applied in liquidation of the partnership debts, including the claims of partners." [2] The suggestion [3] is purely fanciful that it grew "out of the peculiar law of inheritance there," in the attempt "to remedy the hardship of the rule which excludes all but the eldest child from the inheritance, and from the other rule which exempts real estate in the hands of the heir from all but the specialty debts of the ancestor."

(*a*) *The American Rule.* — A learned English author has expressed the opinion that the rule of out and out conversion, now embodied in the statute, was well settled by judicial decisions, "and may safely be accepted in

[1] Partnership Act, §§ 22 and 20 (2).

[2] Lindley on Part. (5th ed.), *343.

[3] Repeated in Darrow *v.* Calkins, 154 N. Y. 503; 49 N. E. 61 (1897).

other common law jurisdictions."[1] Such is not the view, however, of the American courts.

In the case last cited it was said: "The clear current of the American decisions supports the rule that, in the absence of any agreement, express or implied, between the partners to the contrary, partnership real estate retains its character as realty with all the incidents of that species of property between the partners themselves, and also between a surviving partner and the real and personal representatives of a deceased partner, except that each share is impressed with a trust implied by law in favor of the other partner, that, so far as is necessary, it shall be first applied to the adjustment of partnership obligations and the payment of any balance found to be due from the one partner to the other on winding up the partnership affairs. To the extent necessary for these purposes, the character of the property is, in equity, deemed to be changed into personalty. On the death of either partner, where the title is vested in both, the share of the land standing in the name of the deceased partner descends as real estate to his heirs, subject to the equity of the surviving partner to have it appropriated to accomplish the trust to which it was primarily subjected. The working out of the mutual rights which grew out of the partnership relation does not seem to require that the character of the property should be changed until the occasion arises for a conversion, and then only to the extent required. The American rule commends itself for its simplicity. It makes the legal title subservient in equity to the original trust. It disturbs it no further than is necessary for this purpose. The portion of the land not required for partnership equities retains its character as realty, and it leaves the laws of inheritance and descent to their ordinary operation."

[1] Pollock's Digest of Part. (5th ed.), 65, *n.* 1.

5. Rights of Firm Creditors to Firm Realty. — Both in England and in this country the creditors of the firm can compel the application of partnership real estate to the payment of their claims. In England, upon the death of one partner, the legal estate in real property jointly owned by the partners devolves on the surviving partners, who can sell or mortgage it in winding up the affairs of the firm,[1] and convey a perfect title thereto.

In this country, the surviving partners, in such cases, can dispose of the property; but under the doctrine stated in Darrow *v.* Calkins, they cannot convey the legal title. They can, however, transfer full equitable ownership, and confer upon the purchaser the right to the aid of a court of chancery to compel the heir or devisee of the deceased partner to convey his legal title.[2]

These rights of the firm creditors are not affected by the fact that the firm realty stands in the name of a partner to whom the firm is indebted.[3]

6. Creditor Partner's Rights against Firm Realty. — Not only is the real estate of a firm treated as personalty, for the purpose of paying outside creditors of the firm, but it is also deemed converted into personalty for the purpose of adjusting the equities of the partners. If one partner, upon the settlement of the firm's affairs, is a creditor to the extent of the value of all the real property of the firm, he will be entitled to a decree for its sale and the application of the proceeds to the payment of his claim, to the exclusion of the heirs and separate creditors of his copartners.[4]

[1] Re Clough, 31 Ch. D. 324 (1885).

[2] Delmonico *v.* Guillaume, 2 Sand. Ch. 366 (1845); Burdick's Cases on Part. 161; Shanks *v.* Klein, 104 U. S. 18 (1881).

[3] Goldthwaite *v.* Janney, 102 Ala. 431; 15 So. 560 (1894); Burdick's Cases on Part. 176.

[4] Moore *v.* Wood, 171 Pa. St. 365; 33 At. 63 (1895).

7. Dower in Firm Realty. — Under the rule of out and out conversion, the right of dower in partnership real estate does not exist. Under the American rule, however, this right cannot be disposed of quite so summarily. It undoubtedly attaches with all its common law incidents to any real estate of the firm, which remains after the payment of partnership debts and the adjustment of the partners' equities. Whether it attaches as soon as land is acquired by the firm, subject to the claims of firm creditors, or whether it does not come into existence until "the partnership is terminated and wound up by judgment or agreement, and it is determined that the land no longer forms part of the partnership stock, and is not required for its purposes,"[1] is a question upon which our courts are not agreed.

According to the New York decisions, it probably attaches at once.[2] Hence the wives of partners ought to join their husbands in conveyances of firm realty, and should be made parties to a bill for an account or for the sale of such realty to pay debts,[3] in order to give the purchaser a perfect title. According to other American decisions the wife has no inchoate right of dower during the existence of the partnership. Only so much of firm realty "becomes the individual real estate of the partner as remains *in specie*, unconverted, after all the purposes of the partnership have been entirely fulfilled; and it is

[1] Woodward-Holmes Co. *v.* Nudd, 58 Minn. 236; 59 N. W. 1010 (1894); Burdick's Cases on Part. 179.

[2] Fairchild *v.* Fairchild, 64 N. Y. 471 (1876). A similar view obtains in Massachusetts. The legal estate vests in the partners as tenants in common, yet it is held by them in trust for the purposes of the partnership. To the extent of this trust, the wife of a partner has no dower rights; but beyond that she is entitled to dower, because her husband holds the surplus as legal estate. Dyer *v.* Clark, 5 Met. 562 (1843).

[3] Pugh *v.* Currie, 5 Ala. 446 (1843).

only to such of it that any inchoate interest of the wife attaches." [1]

(*a*) *Reasons for Limiting Right of Dower.* — This view is based on the nature and necessities of a partnership. In the last cited case it was said that, if the inchoate right of dower attached to firm real estate upon its acquisition, "the partners could never, even during the active life of the copartnership, convey perfect title to partnership land without their wives joining, except to the extent actually necessary to pay existing debts of the firm. This would practically involve, in every case where one of the wives refused to join in a conveyance, the necessity of a suit, to which she is made a party, in order to determine whether the sale was necessary to pay debts. Any such rule would hamper the business of the firm to an extent that might practically defeat the purposes of the partnership."

The court, therefore, decided that the purchaser of real estate from a firm obtained a perfect title thereto, although the wife of a partner had not joined in the conveyance, nor had been made a party to the suit for the dissolution of the firm and the sale of its property, and although the proceeds of the real estate were in excess of the firm's debts.

8. Out and Out Conversion by Agreement of Partners. — Even in this country, firm realty may be converted into personalty, for all purposes, by the agreement of the partners. This agreement is embodied at times in the partnership articles. A stipulation, "that all the real estate whatever belonging to the said firm shall be, and is hereby, considered as part of the joint stock and funds of said firm, and as possessing all the incidents and liabilities of partnership funds and personal property, and is hereby by the parties fully impressed with

[1] Woodward-Holmes Co. *v.* Nudd, *supra.*

such incidents and liabilities," works a total conversion of the realty into personalty, and enables the surviving partner to convey a perfect legal title thereto.[1]

A deed from one partner of all his right, title, and interest in firm real estate to his copartner, to be held by the grantee as partnership property, with power to manage, sell, and distribute the proceeds as firm stock, works an out and out conversion into personal property, at least as between the partners and their representatives.[2] Such a deed does not create a trust in lands. "It recognizes a pre-existing trust imposed upon the lands, implied by law, and arising out of the partnership relation, and that the trust is to continue notwithstanding the conveyance of the legal title."

In such cases, the intention of the parties to work an out and out conversion is clearly expressed. But effect ought to be given to the intention of the partners, in whatever manner it may be disclosed. When real estate is purchased with firm funds and is treated by the partners as a part of the firm assets, an agreement for conversion may well be inferred.[3]

9. Exempt Property. — Under statutes which exempt certain property of debtors from legal process, the firm, as such, has no rights. They are intended for the benefit of natural persons only.[4] Although these statutes are humane in their object, and are entitled to a liberal construction, most courts have felt constrained to hold that they do not secure to the individual partner any exemption

[1] Davis *v.* Smith, 82 Ala. 198 (1887); Burdick's Cases on Part. 182.

[2] Darrow *v.* Calkins, 154 N. Y. 503; 49 N. E. 61 (1897).

[3] Denio, J., in Collumb *v.* Read, 24 N. Y. 505 (1862), approved in Darrow *v.* Calkins, *supra.*

[4] *Cf.* Betts *v.* Letcher, 1 S. D. 182, 201; 46 N. W. 193 (1890), where it is said: "It is true, the exemption belongs to the firm . . .; yet each partner is entitled to his several interest in that exemption, according to the number and interest of the partners."

out of firm property. They provide that certain articles owned by him, such as "tools and implements," "materials and stock in trade," "a team," "household and kitchen furniture," and the like, necessary for the prosecution of his business or the support of his family, or property owned by him not exceeding a certain sum, or a homestead, shall not be taken from him by his creditors under attachment, execution, or in bankruptcy proceedings.

In all cases, however, it is a portion of his property that is exempted. "But property belonging to the firm cannot be said to belong to either partner as his separate property. He has no exclusive interest in it."[1] "In case of a partnership, neither member has title to firm property, but the title is in the firm."[2] It is clear, therefore, upon principle, that one who transfers to a firm property which would be exempt from process if he retained the ownership of it, loses the benefit of the statutory exemption, as he would lose it if he transferred it to a third person.

(*a*) *Anomalous Decisions.* — A few courts maintain a different doctrine. They have treated the partners as tenants in common of the firm property, and have accorded to them the statutory privilege which would undoubtedly be theirs if their titles to the partnership property were several.[3] Occasionally a court has accorded the statutory exemption to a partner against his separate

[1] Pond *v.* Kimball, 101 Mass. 105 (1869); Burdick's Cases on Part. 186.

[2] Green, Huffaker, & Co. *v.* Taylor & Son, 98 Ky. 330; 32 S. W. 945 (1895); Burdick's Cases on Part. 113.

[3] Skinner *v.* Shannon, 44 Mich. 86; 6 N. W. 108 (1880). In some of the cases, which are generally cited as in accord with the last mentioned decision, the true relation of the so-called partners appears to have been that of common owners of chattels, and not of partners. Radcliff *v.* Woods, 25 Barb. (N. Y.) 52 (1857), and Stewart *v.* Brown, 37 N. Y. 350 (1867), are of this class.

creditor, while denying it to him against firm creditors, on the ground that "partnership debts have a superior claim to partnership assets."[1] It is said that, if a partner has an interest in firm property which could be levied upon under an execution against him alone, he has such an interest as should entitle him to his exemptions out of it; that it is no concern of the officer that the entire title to the property is not vested in the judgment debtor, and that the title of the copartner and the superior claims of firm creditors will not be affected by according the exemption and setting aside the statutory allowance.[2]

### § 3. Firm Title devested by Act of the Firm.

That a firm may dispose of its property in the ordinary course of trade is unquestioned. To make such transfers is one of the purposes for which it is organized. Can it dispose of its property to one or more of its members, thereby converting joint ownership into separate ownership? The question received an affirmative answer in the leading case of Bolton *v.* Fuller.[3]

A firm of four persons carried on a banking business in Liverpool. Two of them carried on a separate banking house in London. Upon the bankruptcy of both partnerships, it was held that bills of exchange deposited with the Liverpool bank, and by it discounted with the London bank, were the property of the latter; and that the acceptor could not recover them, although the arrangement under which he had deposited the bills with the Liverpool bank was such as would have entitled him to their surrender had they remained its property. Partners, it was

[1] Dennis *v.* Kass & Co., 13 Wash. 137; 39 Pac. 656 (1895).

[2] The power of partners to secure the right to exemptions by converting partnership assets into their separate property depends upon the principles which are discussed in the next section.

[3] 1 Bos. & P. 539 (1796); Burdick's Cases on Part. 187.

declared, "may by their acts convert the joint property of the general partnership into the separate property of an individual partner, or into the joint property of two or more partners, or *e converso*. And their transactions in this respect will, generally speaking, bind third persons, and third persons may take advantage of the same, in the same manner as if the partnership were transacting business with strangers."

1. FIRM PROPERTY MAY BECOME THE SEPARATE PROPERTY OF A CONTINUING PARTNER. The dissolution of a firm is often accompanied by an agreement for the purchase of the business by one or more of the partners. Upon the execution of such a contract in good faith, the firm property becomes the separate property of the purchasing member or members.[1] "If," said Lord Eldon, in the case last cited, "the court should say that what has ever been joint or separate property shall always remain so, the consequence would be that no partnership could ever arrange their affairs."

Without regard to this "argument of inconvenience," which Lord Eldon thought entitled to great consideration, it seems perfectly clear that all of the partners can, by their joint act, transfer the firm title to any partner, subject to the right of firm creditors to impeach the conveyance for fraud. "They have power to dispose of the *corpus* of the joint property; and the exercise of that power, when free from fraud, devests the title of the firm as effectually as if they had united in a sale to a stranger."[2] The sale of one partner's interest to his copartner, in a firm of two, transforms firm ownership into separate ownership; but the sale of one partner's interest to an-

[1] Ex parte Ruffin, 6 Ves. 119 (1801); Burdick's Cases on Part. 192.

[2] Menagh *v.* Whitwell, 52 N. Y. 146 (1873); Burdick's Cases on Part. 222.

other partner, in a firm of three or more, does not affect the firm title.[1]

by partners, inter se.

(*a*) *Executory Agreement for Conversion.*—Although the partners may have bound themselves by contract to convey the firm assets to one or more of their number, such contract will not work the conversion of firm property into separate property, as against firm creditors, so long as it remains executory. Accordingly, if it is agreed that one partner shall receive a certain sum for his interest in the firm, and bills of exchange for that sum payable to the order of the firm are handed to him unindorsed, they will be treated as firm property, and available to firm creditors, in case the firm becomes insolvent before indorsement.[2] Even though the partners have agreed upon a division of firm property, and have taken possession of their allotted portions, if the delivery was upon condition that security should be given by one of the purchasers, the conversion will be deemed not consummated until such condition is performed.[3]

It often happens, however, that the purchaser promises to do acts which are not conditions of the passing of the firm title to him. In such cases, the mere fact that he has not performed his promise will not arrest the conversion of firm property into separate property.[4] "The test," in such cases, in the language of an eminent authority,[5] "is to see whether there was at the time of the bankruptcy any act still to be done before the ownership could be considered by the partners as changed; if in any case there

[1] Ex parte Burnaby (1746), Cooke's Bankruptcy Law, 244; Menagh *v.* Whitwell, *supra*.

[2] In re Kemptner, L. R. 8 Eq. 286 (1869); Burdick's Cases on Part. 196.

[3] Fitzgerald *v.* Cross, 20 N. J. Eq. 90 (1869).

[4] Mofflyn *v.* Hathaway, 106 Mass. 414 (1871).

[5] Lindley on Part. (5th ed.), *699.

was such an act to be done, the trustee will not be bound by the agreement, whilst if there was not, he will."

It is well to bear in mind also the following comments of a learned English judge on this class of cases: "But the struggle of the courts has always been to find some loophole for the benefit of creditors; and if the transfer were not itself absolute, or if it wanted any of the formalities required by law or equity to render it valid, the courts have readily laid hold of any of the circumstances to bring back the property into a just course of distribution among the general creditors, who would have been entitled to a lien on it but for the attempted transfer." [1]

2. Conversion must be in Good Faith. — While the title to firm property may be transferred from the firm to its members, the creditors of the firm have the right to impeach the transfer for bad faith. In case the firm of A., B., & C. conveys its property to a partnership composed of A. & B., in satisfaction of a debt claimed to be due from the former firm to the latter, the transaction "should be carefully scrutinized by the courts, . . . and set aside, . . . unless affirmatively it is clearly shown that the transaction was free from fraud." [2] A. & B., it was said, in the last mentioned case, stood in the relation of trustees towards the firm of A., B., & C., in appropriating the property of the latter firm to the payment of their claim, and had the burden of showing affirmatively the *bona fides* of their claim against their *cestui que trust*.[2]

(*a*) *What is meant by "Good Faith."* — While the authorities are agreed that "good faith" is essential to the

[1] Sir G. Rose in In re Fear, 4 D. & Ch. 56 (1834).

[2] Bonwit *v.* Heyman, 43 Neb. 537; 61 N. W. 716 (1895); Burdick's Cases on Part. 192, note. In this case the transfer was made without C.'s assent, and to a creditor of the firm of A. & B. to whom they had assigned their claim against A., B., & C.; but the ground of decision is fairly stated in the text.

conversion of firm property into separate property, they use the term in various significations.

Some courts limit it to the state of mind of the purchaser. They appear to confine the inquiry to the domain of morals and to apply the proverb, "For as he thinketh in his heart so is he." Accordingly, they sustain a transfer of firm property to an honest creditor of one partner, if made with the assent of all of the firm, even though the transfer left the firm and its members insolvent, and was made by them with fraudulent intent against the partnership creditors.[1]

Others extend the term to the state of mind of the transferor and the transferee. If the partners, in case of a sale of the interest of one to his copartners, or if the partners and the creditor of one partner, in case of a transfer of firm property in satisfaction of the individual creditor's claim, have honest intentions, their transfer of firm property is held to be unassailable. Actual fraud, moral obliquity, must characterize the transaction, or it cannot be impeached and set aside by the firm creditors. The transfer is not necessarily fraudulent towards such creditors, it is said, because the firm is insolvent and receives no consideration for the property transferred.[2]

(*b*) *Reasons for Limiting Good Faith to a State of Mind.* — These have been stated in a leading case[3] as follows: "The right of each partner extends only to the share of what may remain after payment of the debts of the firm and a settlement of its accounts. Growing out of the right, or rather included in it, is the right to have

[1] Myers *v.* Tyson (Kan.), 43 Pac. 91 (1896). "There must be participation in the fraud on the part of the grantee, or, at least, knowledge of the intended fraud of the grantor must be shown, or the sale will be upheld."

[2] Purple *v.* Farrington, 119 Ind. 164; 25 N. E. 904 (1889).

[3] Case *v.* Beauregard, 99 U. S. 119 (1878).

the partnership property applied to the payment of the partnership debts in preference to those of any individual partner. This is an equity that partners have between themselves, and in certain circumstances it enures to the benefit of the creditors of the firm. The latter are said to have the privilege or preference, sometimes loosely denominated a 'lien,' to have the debts due to them paid out of the assets of a firm in course of liquidation, to the exclusion of the creditors of its several members. This equity is a derivative one. It is not held or enforceable in their own right. It is practically a subrogation to the equity of the individual partner, to be made effective only through him. Hence, if he is not in a condition to enforce it, the creditors of the firm cannot be."

It is true the foregoing doctrine was not necessarily involved in the case then before the court, for the transfer of the firm property was in consideration, in part at least, of the payment of certain firm debts by the transferee; but it has been adopted and enforced by the United States Supreme Court in later decisions,[1] and is undoubtedly the settled rule of law for that tribunal.

It has been accepted by a number of State courts also. In a recent decision, sustaining a mortgage on firm property, given to secure a debt of one of its members, the Supreme Court of Iowa declared: "In joining in the execution of the mortgage securing the payment of the individual indebtedness of Joseph Johnston, the other member of the firm simply waived his right to have the firm property applied to the satisfaction of its debts. This right was for his benefit, and it was his privilege to allow the individual debts of Joseph to be first paid. The order in which the assets of the firm were to be disposed of was sub-

[1] See Huiskamp *v.* Moline Wagon Co., 121 U. S. 310, 7 Sup. Ct. 899 (1886), upholding the transfer of firm property to an individual creditor of one partner.

ject to the determination of the partners. They were supposed to know their respective interests therein, and, having agreed that the property might be appropriated by Joseph Johnston in securing his indebtedness, they are not in a situation to complain. It simply amounted to an understanding, in the absence of any showing to the contrary, that Joseph had an interest in the assets equal at least to the debt secured, and a consent that he might withdraw therefrom to this amount. The agreement that this might be done was certainly valid, as between the partners; and, the consideration as to Joseph Johnston being sufficient, the validity of the mortgage will be upheld."[1]

(c) *Collusive Waiver of a Partner's Lien.* — Even in jurisdictions where the foregoing doctrine prevails, it is generally admitted that the waiver of his lien by a partner, in order to destroy the derivative equity of firm creditors, must be an honest one. If he unites in a conveyance of joint property to a partner or to an individual creditor, "with a knowledge of the insolvency of the firm, and with an intent to deprive the creditors of its proper application to the payment of the joint debts," it "would be in fraud of the law; and equity would at once set it aside."[2] But it has been held that if partners suffer firm property to be sold under a judgment for their joint debt, though not a partnership obligation, their conduct is not collusive and

[1] Johnston *v.* Roebuck, 73 N. W. 1062 (1898).

[2] Howe *v.* Lawrence, 9 Cush. (Mass.) 553 (1852). In this case there was no evidence that the partners knew that the firm was insolvent; the continuing partner thought he could carry on the business successfully, and during the month of his separate ownership he added five or six hundred dollars' worth of goods to the stock. Following the extract in the text is this statement by the court: "It is only when partners act fairly for the purpose of dissolution and winding up the affairs of the firm, that creditors will be bound by a change of the partnership property to the separate estate of one of the partners."

fraudulent, "and the purchaser takes an absolute title, free from all claims of partnership creditors."[1]

3. Bona Fide Transfer requires a Consideration to the Firm. — A transfer of partnership property in payment of the separate debt of a partner, for which neither the firm nor the other partners are liable, is a voluntary conveyance, and clearly impeachable by the creditors of the firm as well as by the creditors of the other partners, if it leaves the firm and such partners insolvent.[2] And this doctrine is enforced generally by the courts.[3]

But suppose the partners unite in a conveyance of firm property to pay or secure the separate debts of each. Will the fact that they are equally benefited by the transfer render it valid as against firm creditors? Surely not upon principle; and yet such a conveyance has been upheld in a recent case.[4] So confident was the court of the

[1] Rouss *v.* Wallace (Col.), 50 Pac. 366 (1897). "But," added the court, "while a sale in such case of the partnership effects, by transferring the title of the partners in the property seized, carries their equities with it, and so extinguishes the right to a preference of firm creditors, who prior to the sale have acquired no liens upon the property, we do not think that the mere levy of an execution or attachment upon the partnership property in favor of creditors of the individuals would injuriously affect the right of creditors of the partnership. Upon the fact of the levy no waiver of the equities of the partners could be predicated. Acts of waiver must be voluntary, but submission to the levy of a writ is compulsory. It is only where there has been a complete divestiture of their title and possession that their equities are destroyed by legal process; so that, as against the partnership creditors, the levy creates merely a lien upon the interests of the several partners in the partnership property, and those interests attach only to what may remain after the firm debts have been paid. In our opinion, partnership creditors levying subsequently, but before sale, would still be entitled to preference in the distribution of the assets."

[2] Wiggins *v.* Blackshear, 86 Tex. 670; 26 S. W. 930 (1894); Burdick's Cases on Part. 198.

[3] Wilson *v.* Robertson, 21 N. Y. 587 (1860).

[4] Wiggins *v.* Blackshear, *supra.*

correctness of its view that it declared "no one would doubt the perfect right of partners," in such a case, "under agreement between themselves, to pay or secure their several debts with partnership assets, for this would be simply using by each one what belonged to him for a lawful purpose."

The error of the court is in treating a partner's share in a firm as the interest of a tenant in common in the firm stock; when in truth it "is his proportion of the partnership assets after they have been all realized and converted into money, and all the debts and liabilities have been paid and discharged."[1] The court said: "The value of the firm assets, exclusive of accounts and claims, which amounted to $800, was shown to be $1,310, and one half of this was more than the individual indebtedness of either partner secured by the mortgage. As partnership creditors had no lien on firm property, no reason is perceived why each member might not lawfully permit the other to pay his individual debt out of his own share of the partnership property." The court appears to have forgotten that whether each partner was paying his separate creditors out of his own property could be determined only after the conversion of the mortgaged stock and the accounts into cash, the discharge of firm debts, and the adjustment of the accounts between the partners. His share of this remnant was all that each partner could mortgage to a separate creditor.[2]

(*a*) *Firm Property cannot be diverted from Firm Creditors.* — In a case very similar to that which we have been considering, the Supreme Court of Mississippi[3] adjudged the conveyance invalid as against the creditors

[1] Lindley on Part. (5th ed.), *339.

[2] Bank *v.* Carrollton Railroad, 11 Wall. (U. S.) 624 (1870).

[3] Jackson Bank *v.* Durfey, 72 Miss. 971; 18 So. 456 (1895); Burdick's Cases on Part. 201.

of an insolvent firm. It was insisted by the separate creditors, that each partner had received a full consideration for his release of his right as a partner, in the assent of the other partner to the conveyance. "The reply is," said the court, "that a full consideration does not make a contract, otherwise unlawful, valid. If A. agrees to do an unlawful act if B. will do another, of what avail is it that each will reap a benefit from such an act of the other? Durfey had a right to have the partnership property applied to the partnership debts, and Ascher had a like right. While these reciprocal rights existed, they were of value as property rights of the debtors to a certain class of creditors, i. e. firm creditors. . . . We are unable to perceive any just principle upon which the right of a debtor can be recognized to thus deal with his estate for the very purpose of obstructing his creditors." The same conclusion has been reached in New Jersey,[1] and is supported by the great weight of authority both in England[2] and in this country.

In some jurisdictions the invalidity of such a conveyance has been based on the ground that "a partnership in contemplation of law is an entity distinct from the members who compose it."[3]

4. Assumption by the Firm of Separate Debts. — While a firm is solvent, it may lawfully assume the debts of its members. If this is done, a subsequent conveyance of firm property for the payment of such debts is valid, even though the firm is then insolvent.[4] So, if a firm

[1] Bannister *v.* Miller, 54 N. J. Eq. 121, 701; 32 At. 1066 (1895); Burdick's Cases on Part. 207.

[2] Ex parte Mayou, 4 DeG. J. & S. 664 (1865).

[3] Teague *v.* Lindsey, 106 Ala. 266; 17 So. 538 (1895); Burdick's Cases on Part. 207 *n.*

[4] Nordlinger *v.* Anderson, 123 N. Y. 544; 25 N. E. 992 (1893); Teague *v.* Lindsey, *supra.*

receives a valuable consideration for its assumption or guaranty of its members' debts,[1] its transfer of firm property in satisfaction thereof cannot be impeached by its other creditors. Such liabilities are as truly partnership debts as those which are incurred for goods bought by the firm.

5. Promise of Purchasing Partner to pay Firm Debts. — As between the partners, a sale of his interest by one to the other, in consideration of the promise by the purchaser to pay the firm debts, is binding, and works a conversion of firm property into separate property. Whether it will have the same result, as respects firm creditors, is to be determined by applying the principles which we have been discussing.

If the members are insolvent, and directly after the sale the purchaser becomes bankrupt or makes an assignment for the benefit of creditors, the necessary result of the transfer would be to postpone the claims of partnership creditors against the property to those of the purchaser's separate creditors. Moreover, as the purchaser is insolvent, his promise to pay the firm debts cannot be considered a valuable consideration to the firm for the transfer of its property to him. Such a transfer, therefore, ought to be held invalid as against firm creditors.

In the language of Lord Chancellor Westbury:[2] "Taking then, in the first place, the principle of law which is embodied in the statute of 13 Eliz. c. 5, and applying that to the transaction, I think that it was not competent for the one to make or for the other to accept an assignment of that description, both of them being insolvent at the time, . . . because it had for its immediate and necessary object and consequence the alteration of the property in

[1] Bernheimer *v.* Rindskopf, 116 N. Y. 428; 22 N. E. 1074; 15 Am. St. R. 414 (1889).

[2] Ex parte Mayou, 4 DeG. J. & S. 664 (1865).

such a manner as would defeat or delay the joint creditors. . . . Having regard to the principle that a voluntary assignment is, in this sense, a fraudulent assignment, if I regard the transaction as entered into by one partner alone, I cannot look at it as a conveyance for good or valuable consideration, seeing that the covenant by the assignee of the partner was a covenant entered into by a man in a state of insolvency, and in this sense, being voluntary, it would be fraudulent within the meaning which has been applied to this term."

(a) *When Firm Creditors are not Defrauded.* — The transfers which we are now considering, cannot defraud firm creditors if either partner remains solvent and within the jurisdiction, for their claims can be collected from him. Nor do they necessarily defraud such creditors where the property remains in the possession of the purchasing partner for several months. As it is still subject to legal process in favor of such creditors, the transfer does not of itself hinder, delay, or defeat them.[1] If, however, before they can obtain a levy in the ordinary course of litigation, separate creditors of the purchasing partner seize it, or the purchaser becomes bankrupt or makes an assignment for the benefit of creditors, the transfer does operate to hinder, delay, and defeat the creditors of the firm, and should be held fraudulent as against them.

The right of firm creditors to have the assets of a partnership, whose members are insolvent, applied to the payment of their claims before the assets "can be devoted either to the separate use, or appropriated to the payment of the separate debts of any of the members of the firm," is a property right of these creditors which cannot be destroyed by the partners.[2] This view, as we have seen, is

[1] Stanton *v.* Westover, 101 N. Y. 265 (1886); Wiggins *v.* Blackshear, 86 Tex. 670 (1894); Burdick's Cases on Part. 198, 200.

[2] Franklin Sugar Refining Co. *v.* Henderson, 86 Md. 452; 38 At.

sustained by the great weight of authority.[1] It is rejected, however, in those jurisdictions which make the test of the legal *bona fides* of a transfer, the state of mind of the parties thereto.[2] p. 98.

(*b*) *Sale by one Partner to Others, with Reservation of his Lien.* — In some cases, contracts of sale between partners have been treated by the courts as conditional and not absolute transfers. Thus they have been brought within a principle already discussed,[3] and firm creditors have been permitted to subject the property in the hands of the purchasing partner to the payment of their debts. In such cases it has been "held that the agreement to pay the debts as a consideration for the transfer was a sufficient recognition of the equitable lien of the partnership creditors, tracing the same, through the equity of the vendor, to enable them, joining with him, to enforce such equity."[4]

If the transfer is made subject to firm debts, the rights of creditors are thereby expressly preserved.[5] In the case last cited, the New York Court of Appeals declared: "The partnership, as such, has its own property and its own creditors, as distinct from the individual property of its members and their individual creditors. The firm creditors are preferentially entitled to be paid out of firm assets. Whatever may be the true foundation of the equity, it is now an undisputed element in the security of the firm creditors. The insolvent firm cannot apply the

991 (1897); Bartlett *v.* Meyer-Schmidt Grocer Co., 65 Ark. —; 45 S. W. 1063 (1898).

[1] Darby *v.* Gilligan, 33 W. Va. 246; 10 S. E. 400; 6 L. R. A. 740 (1889).

[2] In addition to cases heretofore cited on this point, see Wilcox *v.* Kellogg, 11 Ohio, 394 (1842).

[3] *Supra*, p. 196.

[4] Thayer *v.* Humphrey, 91 Wis. 276 (1895); Burdick's Cases on Part. 117, 123, citing Olson *v.* Morrison, 29 Mich. 395 (1874).

[5] Bulger *v.* Rosa, 119 N. Y. 459; 24 N. E. 853 (1890).

firm assets in payment of the individual debts of the partners, nor can the equity of the firm creditors be defeated by an attempted conversion of the assets of the firm into the individual assets of one of the partners, through a transfer by one partner of his interest therein to the other. In either of the cases supposed, they would remain, as to the firm creditors, firm assets, which could be followed and taken on execution by firm creditors until they had come to the hands of a *bona fide* purchaser; and where an individual creditor of one of the members of an insolvent firm, knowing of such insolvency, takes a transfer of firm property in payment of an individual debt, his act is not merely a violation of an equitable right of the firm creditors, but it constitutes a fraud under the statute of Elizabeth. The law regards it as a voluntary transfer, made to hinder, delay, and defraud the firm creditors, and as to them is void."

### § 3. (A.) Firm Title Devested by Act of one Partner.

"Every partner is an agent of the firm and his other partners for the purpose of the business of the partnership."[1] This relation of each partner to the firm and to his associates results from the very nature of partnership. It was recognized by the custom of merchants, and has never been questioned by the courts. In the language of an early writer, "Partners may be imagined virtually present at and sanctioning the proceedings they singly enter into in the course of trade; or as each vested with a power enabling them to act at once as principals and as the authorized agents of their copartners. It is for the advantage of partners themselves that they are thus held liable, as the credit of their firm in the mercantile world is hereby greatly enhanced, and a vast facility is given to all their dealings; insomuch that they may reside in dis-

[1] British Partnership Act, 1890, § 5.

tant parts of the country or in different quarters of the globe."[1]

1. Each Partner may sell Firm Goods. — In one of the earliest reported cases bearing upon partnership law, "it was agreed by the court that the sale of one partner is the sale of them both";[2] and more than a century ago Lord Mansfield laid it down as unquestioned law that "each has a power singly to dispose of the whole of the partnership effects."[3]

The only limitation upon the power of a partner to transfer the firm title to a stranger is, that it shall be exercised "for the purpose of the business of the partnership." If the business of the firm consists in buying and selling goods, any partner has the power to dispose of the entire stock to a *bona fide* purchaser.[4] He has the power, also, of paying the debts of the firm; and payment may be made with firm money, or with firm goods which have not been converted into cash. Moreover, as the firm has the legal right to pay one creditor in full, to the exclusion of others, it would seem to follow that each partner has the power to exercise this right.

A bill of sale, therefore, of all the partnership stock, at a fair valuation, in satisfaction of an honest claim against the firm, although executed on behalf of the firm by one partner without his copartner's consent, should be held, and has been held, a valid alienation of firm title to the creditor.[5] In some jurisdictions, however, it has been

[1] Watson on Part. (2d ed.), 167. In Mabbett *v.* White, 12 N. Y. 442 (1855), Burdick's Cases on Part. 212, 214, it is said: "This *jus disponendi* of each partner is for the advantage of trade and commerce, and no doubt strengthens the credit and benefits the partners themselves."

[2] Lambert's Case, Godbolt, 244 (1614).

[3] Fox *v.* Hanbury, Cowp. 445 (1776).

[4] The powers of partners will be more fully discussed in the next chapter.

[5] Mabbett *v.* White, 12 N. Y. 442 (1855); Burdick's Cases on Part.

ruled that in case one partner undertakes to dispose of the entire stock, either for cash or in satisfaction of the claim of a favored creditor, the other partner "may protect himself by forbidding or dissenting before the sale is completed."[1] This is based on the doctrine that fair dealing between the partners requires that the copartner, if conveniently accessible and no sudden imperative exigency arises, should be consulted in such cases.

The partnership may be of a character that negatives an implied power of a partner to sell the entire property without the consent of his copartners. Such a sale would not appear to be "for the purpose of the business" of a newspaper partnership[2] or of a firm of attorneys.

2. Either Partner may Mortgage Firm Goods. — The reasons for upholding a sale of firm property by a partner have induced the courts to sustain chattel mortgages given by him, either to raise money for the firm or to secure firm debts. Here, again, the only limitation upon his implied power is the nature of the partnership business. In case of an ordinary trading partnership, his implied authority to pledge or mortgage firm goods in order to raise money for the firm business, or to secure existing partnership debts, is unquestioned, even though the pledge or mortgage extends to the whole of the firm stock. Nor does it matter that the chattel mortgage executed by one partner is in the form of a deed. If without a seal it would constitute a valid lien on the property, it will be none the less effectual that it has an unnecessary seal.[3]

212. *Cf.* Bender *v.* Hemstrict, 34 N. Y. Supp. 423 (1895), denying the power of one partner to sell the entire stock to a stranger, for the avowed purpose of ending the partnership.

[1] Ellis *v.* Allen, 80 Ala. 515 (1887); Burdick's Cases on Part. 214, *n.*

[2] Sloan *v.* Moore, 37 Pa. St. 217 (1860).

[3] Tapley *v.* Butterfield, 1 Met. (Mass.) 515 (1840); Burdick's Cases on Part. 211.

In the case last cited, Chief Justice Shaw expressed the following opinion concerning a mortgage of firm realty by a partner: "Lands held by partners are considered as lands held by tenants in common; and as one tenant in common cannot pass any estate of his cotenant, and as land cannot pass without deed, it follows that one partner cannot convey away the real estate of the firm without special authority." The principles upou which the effect of such a mortgage depends have been considered at some length in a preceding section,[1] and will be discussed further in the following chapter.

3. Application of Firm Property to a Partner's Debts. — The limitation upon a partner's power to dispose of firm property, which has been referred to repeatedly, precludes him from using it for the purpose of paying his own debts. Accordingly, if a third person is a creditor of the firm as well as of one partner, and receives from such partner a check belonging to the firm, he has no right to apply it to the satisfaction of his claim against the partner, although that may be the older indebtedness. To accord him that option "would be allowing him to pay the debt of one person with the money of others."[2]

Nor would the right of the creditor be enlarged by the express assent of the debtor partner to the application of firm property to the satisfaction of his individual liability. Where the consideration for the transfer of partnership assets is the individual indebtedness of the partner assuming to make the transfer, actual authority from his copartners for his act must be shown, or a case of estoppel against them must be established. "To receive property of a partnership from one of the partners in payment of his personal debt, without the consent of his copartner, is no

[1] *Supra*, Ch. III., § 2.

[2] Thompson *v.* Brown, M. & M. 40 (1827); Burdick's Cases on Part. 211.

less a fraud upon the partnership than to pay a debt due the firm by doing or furnishing something for the personal use of one of its members. Such an arrangement accompanying the receipt of partnership property would be void against the other partner, and would leave the party receiving the property liable upon an implied contract to pay the firm its value."[1] If the property were still in possession of the transferee, it could be reclaimed by the firm or its creditors.[2]

(*a*) *Separate Creditor's Ignorance of Title.* — Even though the separate creditor is ignorant of the fact that the property which he receives belongs to the partnership, he cannot hold it against the firm or its creditors,[3] unless he can make out a case of estoppel. The debtor partner cannot, in his own right, convey title, for he is not the owner of the property. He cannot convey it as agent, for his authority as agent is limited to its transfer for firm purposes. Undoubtedly the firm may estop itself from claiming title as against a separate creditor of the disposing partner. If A. is a secret partner with B. in business carried on in B.'s name, A. holds B. out to the world as the sole owner of the business assets, and as possessing the power of a sole owner to transfer these assets. In such circumstances, a separate creditor of B. who receives a part of the assets in satisfaction of B.'s debt, although it was not contracted in the firm business, is entitled to retain the property.[4]

(*b*) *Doctrine of Lock* v. *Lewis.* — It was upon this doctrine of estoppel that Lock *v.* Lewis [5] was decided, — a case

[1] Brickett *v.* Downs, 163 Mass. 70; 39 N. E. 776 (1895); Burdick's Cases on Part. 215.

[2] Havitey *v.* White, 94 Pa. St. 31 (1880).

[3] Rogers *v.* Batchelor, 12 Pet. (U. S.) 221 (1838).

[4] Swan *v.* Steele, 7 East, 210 (1806).

[5] 124 Mass. 1 (1878).

which is sometimes mistakenly cited for the proposition "that a transfer of firm property in payment of a private debt will not be avoided against a transferee who took the property without knowledge that it was firm property."[1] The plaintiff in that case, upon the dissolution of a partnership between himself and I. L. Robinson and Son, received a note for a part of his interest in the firm from the Robinsons, who continued the business of manufacturing carriages in the name of I. L. Robinson and Son. Later they formed a limited partnership, under the laws of New Hampshire, in the name of I. L. Robinson & Co., in which they were the general partners, and Chase, Parkinson, and Greeley were the special partners. While this partnership was in existence, the Robinsons paid the note to plaintiff by transferring to him three carriages which were the property of the limited partnership, giving him a bill of the goods in the name of I. L. Robinson & Co. Thereafter the carriages were attached by the defendant, a deputy sheriff, under process against the limited partnership, and plaintiff brought replevin. A verdict was ordered for defendant, on the ground that the sale by the two general partners, in payment of their own debt, of goods which were in fact the goods of the partnership, but were not known to the creditor to be such, was void as against the partnership and its creditors.

In setting aside this verdict the Supreme Court was careful to say: "We would not be understood to affirm that the mere belief of the separate creditor that the property which he receives does not belong to the partnership will of itself be sufficient to entitle him to hold it, if there has been nothing in the acts or conduct of the other partners to induce the belief that the partners with whom he dealt were the sole owners. But the evidence before us would warrant a jury in finding, not only that the plaintiff

[1] George on Part. 221, *n.* 50, and see Bates on Part. § 1046.

acted in good faith, but that the active and ostensible partners had been held out as the sole owners of the property."[1] And the conclusion of the court is stated as follows: "For these reasons, we are of opinion that the jury should have been instructed that if the plaintiff, by the manner in which the general partners dealt, and had been allowed by the special partners to deal, with the property sold to him, was induced to believe that it was the property of the general partners only, and, acting on such belief, bought it in good faith, and with no notice or knowledge that the special partners, or any other person than the general partners, had any interest therein, he was entitled to maintain this action."

4. General Assignment by one Partner. — Whether one partner can devest the firm title by a general assignment for the benefit of creditors, is a question upon which the decisions are somewhat conflicting. From the power possessed by each partner to sell all the property of a trading firm to its creditors in payment of debts, it has been argued by some courts that his agency to assign the property to a trustee for sale and distribution among creditors also results from the partnership relation.[2]

The view generally entertained, however, is that a transfer of all the firm property to a trustee for creditors is not an act done "for the purpose of the business of the partnership," but is necessarily and intentionally destructive of

[1] It is submitted that no evidence of this character appears in the statement of the facts by the court. On the other hand, it appears that the firm name, in which the bill of the goods was given, differed from that in which the note was given; and that, upon the formation of the limited partnership, a certificate giving the names of its members as well as the name of the new firm was recorded and published, as required by the statute. *Cf.* Janney *v.* Springer, 78 Iowa, 617; 43 N. W. 461 (1889).

[2] Deckard *v.* Case, 5 Watts (Pa.) 22 (1836); Scruggs *v.* Burruss, 25 W. Va. 670 (1885).

that business, and that an agency to do such an act does not result from the partnership relation.[1]

(*a*) *Actual Authority must Exist.* — If all of the partners are within the jurisdiction and accessible, the partner who would make a valid assignment for creditors must secure their assent or ratification. In case the unauthorized assignment is ratified by the other partners, it will not affect a lien of firm creditors acquired during the interim.[2]

The assent need not be directed to the special act of assignment. If a partner, upon leaving the jurisdiction, writes to his copartner, "Take charge of everything in our business, close it up speedily," he authorizes the latter "to make such disposition of the partnership property as should be deemed most expedient to close up the partnership enterprise," including an assignment for creditors.[3]

The temporary absence of a partner, however, cannot be construed as an implied assent to an assignment executed by his copartner during that period;[4] but his permanent absence and total inattention to the business may warrant the inference that "he intended to intrust the affairs of the firm wholly to the resident partner. . . . He might reasonably expect and be held to intend that the

[1] Osborne *v.* Barge, 29 Fed. 725 (1887).

[2] Stein *v.* La Dow, 13 Minn. 412 (1868). In Adee *v.* Cornell, 93 N. Y. 572 (1883), Bellows and Hunt made an assignment of the firm property of Charles Bellows & Co. A firm creditor obtained judgment against them, and procured the appointment of a receiver of their property in supplementary proceedings. The receiver then brought a suit to set aside the assignment on the ground that Leach and Hinds were secret partners with the judgment debtors, and had not joined in the assignment. The court said: "Even if they were partners, they could ratify an assignment by the other members of the firm, and no one else would have the right to complain."

[3] Wells *v.* March, 30 N. Y. 344 (1864).

[4] Wetter *v.* Schlieper, 4 E. D. Smith (N. Y.) 707 (1858).

member placed in control should not only exercise the implied powers of agency ordinarily possessed by a partner, but, in addition, should have the discretionary power in case of emergency to do what, under the circumstances, should appear to be just and proper in the disposition of the firm property."[1]

(*b*) *A Reasonable Requirement.* — The rule which requires either the express or implied assent of all the partners to a general assignment by a single partner is a perfectly reasonable one. The refusal of such assent by any partner need not result in the sacrifice of firm property. In case of hostile attacks by creditors, a partner who wishes to prevent them from forcing a sale under execution may institute a suit in equity for the dissolution of the partnership and the ratable distribution of its assets among its creditors.[2] Hence, a power in each partner to make an assignment in trust for creditors is not necessary for the protection of the interests of the firm or the rights of its creditors.

### § 3. (B.) Firm Title not Devested by Sale of a Partner's Interest.

The interest of a partner in the firm property is not that of a common law tenant in common. As already pointed out, it is only " a share of what may remain after payment of the partnership debts and after a settlement of the accounts between partners."[3]

Upon the sale of a partner's interest, therefore, all that passes to the purchaser is such share ; the firm title is not

[1] H. B. Claflin & Co. *v.* Evans, 55 Ohio St. 31 ; 45 N. E. 3 (1896) ; Burdick's Cases on Part. 216.

[2] Holmes *v.* McDowell, 15 Hun (N. Y.) 585 (1878) ; Burdick's Cases on Part. 434.

[3] Bank *v.* Carrollton Railroad, 11 Wallace, 624 (1870).

devested. Up to this point there is entire concurrence of authorities.

1. Successive Sales of all the Shares. — It would seem to follow that the firm title is not devested, although the interest of each partner is sold; and such is the holding of the best considered cases on this subject.[1] In the case cited in the last note, each of the five partners who composed the firm of J. C. Smith & Co. had transferred his interest in the firm assets; but there had been no joint act of all the partners relating to these transactions. After these several transfers, and when the firm assets were in the possession of the transferees who claimed title thereto, the sheriff, under an execution in favor of a firm creditor, levied upon the property and sold it. The plaintiff, who had acquired all of the rights which passed under the transfers from four of the five partners, sued the sheriff for conversion. The referee before whom the action was tried decided that, at the time of the levy, neither of the partners defendants in the executions had any leviable interest, and that the judgment creditor had no lien on the firm assets, but that the property belonged four fifths to the plaintiff and one fifth to Mary B. Goodwin, the transferee of the fifth partner. This decision was reversed by the Court of Appeals on the ground that "the title of the firm, as between it and its creditors to the *corpus* of the property, or at least to so much of it as is necessary for the debts, was not devested by the separate transfers to strangers."

The court did not recognize any lien of partnership creditors upon the firm property. On the other hand, it asserted that the firm had power to dispose of its assets; but it denied that the individual members had exercised any such power. The transfers of their interests for their

[1] Menagh *v.* Whitwell, 52 N. Y. 146 (1873); Burdick's Cases on Part. 222.

individual purposes, the court declared, were inoperative upon the *corpus* of the property, so long as there were firm debts unpaid, and the property continued in the firm until its title had been devested by some act of the firm.

2. Sale of a Partner's Interest to One of Several Copartners. — Another question which was discussed in Menagh *v.* Whitwell was whether the sale by two of the five partners of their interests to a third devested the firm title. The court decided that it did not; that the purchasing partner acquired by the sale "the same interest in the firm property that any other transferee would have acquired; that is a right as to the two fifths thus purchased to an account, and to share to that extent in the surplus of the property of the firm." The joint act of the three was not the act of the partnership. Undoubtedly, had the remaining three partners carried on the business thereafter as a new firm, their joint act (unless fraudulent against creditors) would have operated to devest the old firm title, and to transfer it to the new firm of three. But no evidence of such a joint act appeared in that case. All that was done by the three, after the sale by the two of their interests, pertained to winding up the affairs of the dissolved firm, and did not amount to the formation of a new one.[1]

(*a*) *The Opposite View.* — Although the foregoing doctrine appears to be unassailable, it has been repudiated in some jurisdictions. The leading case upon this side is Doner *v.* Stauffer.[2]

Doner and others obtained judgments against Howry, of the firm of Howry and Eshelman. Stauffer and others obtained judgments against Eshelman. The executions were levied upon the firm stock, which was sold and the proceeds brought into court. Stauffer and the other separate

[1] See opinion of Allen, J.

[2] 1 P. & W. (Pa.) 198 (1829); Burdick's Cases on Part. 218.

creditors of Eshelman claimed one half of the proceeds, while the creditors of Doner and the firm creditors disputed this claim, on the ground that the firm of Howry and Eshelman was insolvent when the executions were levied, that Eshelman's interest in the firm was worth nothing, and that after the levy Howry and Eshelman made an assignment to trustees for the benefit of firm creditors. Evidence tending to support this defence was excluded by the trial court, and one half of the proceeds was awarded to Stauffer and the other separate creditors of Eshelman, to the exclusion of the firm creditors.

(*b*) *Reasons for this Holding.* — In delivering the opinion of the Supreme Court, Chief Justice Gibson assigned the following reasons for affirming the judgment of the court below: "Now, had the sheriff sold the interest of but one of the partners, the execution creditor would have clearly been entitled to the proceeds. But although he sold the whole stock at one operation on separate executions against both, there was in contemplation of law a separate sale of each. What, then, would have been the effect had these sales been made consecutively? The first in the order of time would have passed the interest of the partner, subject to the equity of his copartner, and the execution creditor would have been entitled to the price. But this equity, together with the remaining interest of the other partner, would have passed by the succeeding sale to the same purchaser, the execution creditor in that instance also taking the proceeds. Can it make a difference, then, that instead of being consecutive these sales were simultaneous? . . . Here, where the shares of the partners are united in the same purchaser every semblance of partnership equities is at an end. As regards the goods in the hands of the purchasers, this is conceded; but the joint creditors insist that the proceeds are to be substituted for the goods, and subjected to the same equities. That might

be done if the proceeds belonged to the partners; but it is not easy to imagine how they are to be treated as the owners of money raised by a sale on executions against them. . . . Here the partners cannot be prejudiced in respect of their claims on each other, the advantage to be gained from an application of the joint effects to the separate debts being mutual and equal. The consequences are precisely the same as if the effects had been sold on an execution against both. We are therefore of opinion that the joint creditors cannot interpose; and, consequently, that the rejection of the evidence, as well as the direction to the jury, was substantially right."

(c) *Doner* v. *Stauffer Criticised.* — Although this reasoning has been followed in other States,[1] it has not escaped deserved criticism even in the jurisdiction of its distinguished author. Judge Sharswood, after pointing out that "altogether too much was conceded when it was conceded that the goods could not be followed into the hands of the purchaser," and that the equity of a partner is not a salable interest at all, adds, "The practical operation of the doctrines set forth in the opinion in Doner *v.* Stauffer would be that the purchaser, though buying an encumbered title under the first execution, by the legerdemain of a second sale under an execution against the other partner, is thereby vested with an absolute unencumbered title, without paying for it; or what is worse, if the second purchaser is a different person, he gets a clear title, and by the same title clears the title of the first purchaser."[2]

(d) *Absurd Consequences of Doctrine in Doner* v. *Stauffer.* — "The injustice and absurdities" of such doc-

[1] Stahl *v.* Osmers, 31 Or. 199; 49 Pac. 958 (1897); Burdick's Cases on Part. 237.

[2] MS. Lectures, as quoted in Parsons (James), Principles of Part. (1st ed.), 303, 304.

trines are set forth by Judge Rapallo in the following language:[1] "Suppose a firm to consist of three members, each having an equal interest, and to be possessed of assets to the amount of $300,000, and to owe debts to half of that amount. The interest of each partner, supposing their accounts between themselves to be even, is $50,000. The members of the firm are individually indebted. One of them sells his share, and receives for it $50,000, which is its actual value; the share of another of the partners is sold out under execution, and brings its full value, $50,000. Thus far one partner remains, and he has an equity to have the firm debts paid; and those who have sold out are protected against those debts. The purchasers of the separate interests are entitled to the surplus only; the joint creditors still have their recourse against the partnership property and the right to levy on such of it as is subject to sale on execution; but before any levy, the remaining partner sells out his individual interest, or it is sold out on execution. According to the doctrine" of Doner *v.* Stauffer, "the firm property is by this last sale relieved from the partnership debts, the two shares first sold are at once changed from interests in the surplus to shares in the *corpus* of the property free from the debts, their value is doubled, and the fund which should have gone to pay the joint debts is, without any consideration, appropriated by the transferees of the individual interests of the partners."

3. Sale of a Partner's Interest in Firm Realty.— If partners hold the legal title to the real estate of the firm as tenants in common, the transfer of a partner's interest therein would work a change in the title, and the firm would be no longer the sole and unconditional owners of the property. That such is not the effect of the transfer

[1] Menagh *v.* Whitwell, 52 N. Y. 146 (1873); Burdick's Cases on Part. 222, 226.

of a partner's interest has been declared by the New York Court of Appeals.[1]

The firm of Wood Brothers took out a policy of insurance on a building which was a part of the firm property. The policy contained the condition that it should be void if the interest of the insured was other than unconditional and sole ownership. Prior to the issue of the policy one of the six brothers composing the firm had made a general assignment of his individual property for the benefit of his separate creditors; and, the building having been destroyed by fire, the insurance company defended an action brought by the firm upon the policy, on the ground that the sole and unconditional ownership was not in the firm when the policy was placed. But the court held: "Since the title to the real estate held by a partnership is in the firm, and not in the individual members of it, . . . the title was not affected by the assignment of one of the members. It still remained firm property, since the assignee had no interest in it as such, and whether the sale or transfer by the individual member was anything more than a mere form, or conveyed anything to the assignee, must depend upon the existence of a surplus after the partnership affairs are adjusted."

4. The Conveyance of a Partner's Interest is not a Void Instrument. — While it is true that the purchaser of a partner's interest in a particular parcel of the firm property cannot, as a rule, form a definite estimate of the worth of his purchase, and his right may turn out to be a barren one, the instrument conveying the interest is not void.[2] It is effective to transfer to the grantee whatever right the grantor would have possessed with respect to

[1] Wood *v.* Am. Fire Ins. Co., 149 N. Y. 382; 44 N. E. 80 (1896); Burdick's Cases on Part. 240.

[2] Patterson *v.* Atkinson, 37 At. (R. I.) 532 (1897); Burdick's Cases on Part. 241.

this property, upon settling the affairs of the partnership. If the firm is not at once dissolved, but continues in business, the grantee's interest will be subject to the subsequent debts of the firm and equities of the partners.[1]

(*a*) *Mortgage by a Tenant in Common.* — If two persons buy and hold property as equal tenants in common, and not as partners, either of them, by mortgaging his share to secure an individual creditor, can give to such creditor a lien on an undivided half interest in the property. This lien will not be subject to the claim of a joint creditor of the owners, even though that claim be for the purchase price of the property.[2]

### § 4. Firm Title after the Death of a Partner.

By the custom of merchants, the common law benefit of survivorship between joint tenants was denied to surviving partners. This custom is recognized, in the earliest reported cases on the subject in England, as a part of the

[1] Receivers of Mechanics' Bank *v.* Godwin, 5 N. J. Eq. 334 (1846); Cavendas *v.* Bulteel, L. R. 9 Ch. 79 (1873). The British Partnership Act of 1890, § 31, declares: "(1) An assignment by any partner of his share in the partnership, either absolute or by way of mortgage or redeemable charge, does not, as against the other partners, entitle the assignee during the continuance of the partnership to interfere in the management or administration of the partnership business or affairs, or to require any accounts of the partnership transactions, or to inspect the partnership books, but entitles the assignee only to receive the share of the profits to which the assigning partner would otherwise be entitled, and the assignee must accept the account of profits agreed to by the partners. (2) In case of a dissolution of the partnership, whether as respects all the partners or as respects the assigning partner, the assignee is entitled to receive the share of the partnership assets to which the assigning partner is entitled as between himself and the other partners, and for the purpose of ascertaining that share to an account as from the date of the dissolution."

[2] State Bank of Lushton *v.* O. S. Kelley Co., 47 Neb. 678; 66 N. W. 619 (1896); Burdick's Cases on Part. 243.

law of the land.[1] Accordingly, it was held that the representative of the deceased partner could avail himself of its benefit, even though the deceased had been advised that the firm stock would survive, and had replied that he was content it should survive.[2]

1. Legal Remedies survive. — Notwithstanding the judicial adoption of the maxim, *Jus accrescendi inter mercatores locum non habet*, it was early decided that, upon the death of a partner, the legal remedies on behalf of the firm survive. In an action of trover, brought by the surviving partner against the converter,[3] and in an action of account similarly brought against a factor of the firm,[4] it was objected that the representative of the deceased partner should have been a party plaintiff; but in both cases it was held that the action must necessarily survive, "otherwise there would be a failure of justice, because the survivors and the executors of those who were dead cannot join in the action, for that their rights are of several natures and there must be several judgments." Upon recovery, however, it was declared to be the duty of the survivor to account to the representative of the deceased for the latter's share. Even in equity, the surviving partner is the proper plaintiff, and need not make the representative of the deceased partner a party, in an action to collect debts due the firm.[5]

2. Legal Title to Firm Assets survives. — Although the survivorship of a firm's legal remedies was firmly established by the early decisions, above referred to, "it is

1 Hammond *v.* Jethro, 2 Brownlow, 99 *n.* (1611); Burdick's Cases on Part. 245.

2 Jeffreys *v.* Small, 1 Vern. 217 (1683).

3 Kemp *v.* Andrews, Carth. 170 (1690).

4 Martin *v.* Crompe, 1 Ld. Ray. 340; Comb. 474; 2 Salk. 444 (1696).

5 Haig *v.* Gray, 3 DeG. & S. 741 (1850); Burdick's Cases on Part. 246.

remarkable that the law" as to the survivorship of the firm's legal title was left in uncertainty until the latter half of this century. As late as 1851, Baron Parke, delivering the unanimous opinion of the Court of Exchequer,[1] declared that there was "no satisfactory authority for the position that the title to partnership chattels survives at law; and the authorities the other way greatly predominate." He even expressed a doubt as to the surviving partner's authority to dispose of firm chattels to pay firm debts, — an authority which is now universally recognized.[2]

But, in the language of Lord Justice Lindley, "all this is of little consequence now,"[3] for both in England and in this country the survivorship of the firm's legal title is well established. An authoritative statement of the present rule in England, on this point, is the following:[4] "The representative of a deceased partner has no specific interest in or claim upon any particular part of the partnership estate. The whole property therein accrues to the surviving partner; and he is the owner thereof, both at law and in equity. The right of the deceased partner's representative consists in having an account of the property, of its collection and application, and in receiving that portion of the clear balance that accrues to the deceased's share and interest in the partnership."[5]

(*a*) *Surviving Partner is not Assignee of Deceased Partner's Interest.* — The title of the firm devolves upon

[1] Buckley *v.* Barber, 6 Exch. 164 (1851).

[2] Lindner *v.* Adams Co. Bank, 49 Neb. 735; 68 N. W. 1028 (1896); Burdick's Cases on Part. 262.

[3] Lindley on Part. (5th ed.), *342, *note x*.

[4] Lord Westbury in Knox *v.* Gye, L. R. 5 H. of L. 656 (1872).

[5] In Taylor *v.* Taylor, 28 L. T. R. 189 (1873), Lord Justice James referred to Baron Parke's statements in Buckley *v.* Barber, *supra*, as "the peculiar views on the subject once taken by the Court of Exchequer."

the surviving partner by operation of law; he is not in any sense the assignee of the deceased partner's interest. The surviving partner, therefore, by virtue of his ownership of a firm judgment, can redeem land from a sheriff's sale, without producing an assignment of the judgment; although the statute governing the case requires that a creditor, claiming a right to redeem under a judgment which has been transferred to him, must file an assignment of such judgment.[1]

(*b*) *Surviving Partner can make a General Assignment.* — As the firm title vests in the surviving partner, he can transfer it to a trustee for the benefit of creditors, without obtaining the consent of the representative of the deceased partner. In this assignment, he may give such preferences among firm creditors as he deems proper.[2] His exclusive power to convert firm assets into cash results from the nature of a partnership. "It was never in the contemplation of the contract of partnership that strangers, as the representatives of a deceased partner are, should have a voice in the determination of questions relating to the distribution of the firm assets among its creditors."[3] Each partner, by the exercise of his *delectus personarum*, has signified his confidence in his copartners to manage the firm's affairs to the exclusion of strangers, and has conferred upon them full authority for such management. If all the firm assets are devoted to the payment of firm debts, it is immaterial to the estate of the deceased partner that some of the creditors are paid in full, while others obtain little or nothing from the firm

[1] Nehbross *v.* Bliss, 88 N. Y. 600 (1882); Burdick's Cases on Part. 246.

[2] Emerson *v.* Senter, 118 U. S. 2 (1885); Burdick's Cases on Part. 253.

[3] Williams *v.* Whedon, 109 N. Y. 333 (1888); Burdick's Cases on Part. 254 *n.*

property. The liability of the separate estate is not increased by preferences among firm creditors.

(c) *Is the Surviving Partner a Trustee?* — That he "is not a trustee in the full and proper sense of that word" is admitted everywhere. The House of Lords has declared that "There is nothing fiduciary between the surviving partner and the dead partner's representative, except that they may respectively sue each other in equity";[1] and Parliament has enacted that, "Subject to any agreement between the partners, the amount due from surviving or continuing partners to an outgoing partner or the representatives of a deceased partner in respect of the outgoing or deceased partner's share is a debt accruing at the date of the dissolution or death."[2]

(d) *Surviving Partner's Quasi Trusteeship.* — In this country, his *quasi* trusteeship has a more extensive character. It is true that the legal title to firm assets is "so completely vested" in him that he may join in the same suit demands due him as an individual and those due him as survivor, and in an action upon a firm claim the defendant can set off a claim against him as an individual.[3] If he is the surviving partner of two firms, he may join demands of both in one suit.[4] Upon his death, the right to settle firm affairs passes to his personal representative.[5] Nevertheless, the representatives of the deceased partner are not limited to the personal liability of the survivor for firm assets. They possess equitable interests therein which the courts will protect and enforce.

[1] Knox *v.* Gye, L. R. 5 H. of L. 656 (1872).

[2] Partnership Act, 1890, § 43.

[3] Holbrook *v.* Lackey, 13 Met. 132 (1847), and cases cited therein; Nehbross *v.* Bliss, 88 N. Y. 600 (1882); Burdick's Cases on Part. 246, and cases cited in the opinion.

[4] Stafford *v.* Gold, 9 Pick. 533 (1830).

[5] Galbraith *v.* Tracy, 153 Ill. 54; 38 N. E. 937 (1894); Burdick's Cases on Part. 257.

(*e*) *Compelling Survivor to apply Firm Property to Firm Debts.* — If the surviving partner neglects his duty of settling the partnership business, or acts in bad faith, "the representative of the deceased partner may invoke the interference of a court of equity, and compel such a disposition of the partnership effects as will be just and proper; this because, as between the partners, and therefore, as between the surviving partner and the personal representative of the deceased partner, the joint assets constitute a fund to be appropriated primarily to the discharge of partnership liabilities."[1]

In case the survivor is insolvent and makes an assignment for the benefit of creditors, the assignee takes whatever remains of the firm assets subject to the same burden or obligation that was impressed upon it in the survivor's hands. If he sells it, the proceeds must be accounted for by him to the representative of the deceased partner. Though the legal title to the firm assets passes to the assignee, they "form a trust fund for the realization so far as possible of the" firm liabilities.[2]

(*f*) *Firm Assets may be reclaimed from a Fraudulent Purchaser.* — In case the surviving partner disposes of the firm assets for less than their value, he may be compelled to account for them at the price which he ought to have obtained. If the purchaser has colluded with him in the sacrifice of the assets, the personal representatives of the deceased may maintain an action against the purchaser "as a wrongdoer and trustee *de son tort*"; and such an action is not barred by an unsatisfied judgment against the survivor in a suit for an accounting.[3] In case

[1] Emerson *v.* Senter, 118 U. S. 2 (1885); Burdick's Cases on Part. 253.

[2] Preston *v.* Fitch, 137 N. Y. 41; 33 N. E. 77 (1893).

[3] Russell *v.* McCall, 141 N. Y. 437; 36 N. E. 498 (1894); Burdick's Cases on Part. 256.

the property remains in the hands of the fraudulent purchaser, the representative of the deceased partner may have a receiver appointed to take the property and apply the proceeds thereof to the satisfaction of partnership claims.[1]

(*g*) *Survivor is subject to a Trustee's Disability to buy Firm Assets.* — In the cases cited under the last heading, the courts refer to the position of a surviving partner in such terms as these: "While he held the legal title, he held it subject to a kind of trust which equity will enforce in favor of those interested in it." "The position is somewhat anomalous, — not exactly and wholly a trustee, and yet not a full owner of the assets which he takes or retains possession of by reason of survivorship."

This *quasi* trusteeship of the surviving partner has been recognized also in cases where his right to purchase firm property has been considered. While it is his duty to settle up the firm's affairs with reasonable promptness, it is also his duty to act fairly and honestly in disposing of firm property. He cannot, consistently with this duty, purchase it from himself, either at public or private sale.[2] If he assumes to buy it, the representatives of the deceased
4. partner can have the sale set aside, or can compel him to account for the property at its fair value.[3] He will not be allowed to make a profit out of his fiduciary position at the expense of the deceased partner's estate, either by purchasing firm assets,[4] or by consenting to the extinguishment of a contract belonging to the partnership and the

[1] Dewey *v.* Chapin, 156 Mass. 35 (1892); Burdick's Cases on Part. 255.

[2] Valentine *v.* Wyser, 123 Ind. 47; 23 N. E. 1076 (1890). In this case it was said the survivor could buy the deceased partner's interest from the representative, as he was not trustee of that interest.

[3] Galbraith *v.* Tracy, 153 Ill. 54; 38 N. E. 937 (1894); Burdick's Cases on Part. 257.

[4] Denholm *v.* McKay, 148 Mass. 434; 19 N. E. 551 (1889).

substitution therefor of one in the profits of which he alone is to participate.[1]

3. It is the Firm Title which Survives. — Notwithstanding the common law decisions,[2] which treat the title of the surviving partner as indistinguishable from his individual title, in equity the two titles are recognized as distinct and independent. This is disclosed in some of the cases already cited.[3] It is brought out still more clearly in the cases now to be considered.

The surviving partner in a banking firm sued the indorser of a promissory note made by the deceased partner, and discounted for him by the firm. The indorser defended on the ground that his indorsement was for the accommodation of the deceased partner, Conrad. This being admitted by the plaintiff, the court declared that defendant was a mere surety for Conrad, "and these facts all being known to Conrad, the partner of plaintiff, in law were all known to plaintiff. This presents a case in which Conrad was both payer and payee, and so far as Conrad was concerned never constituted what is known as a legal cause of action. It could only be adjusted by the partners themselves, in equity, upon a dissolution and settlement of the concern. Neither would it have been the subject of an action at law against the defendant by the firm if Conrad were still living, as the note — the cause of action — would necessarily disclose the equity of the case. The death of Conrad, leaving the plaintiff survivor, does not change the law of the case, and does not authorize the plaintiff to bring an action which he and his copartner would not have had a right to bring if he were living."[4]

[1] Little *v.* Caldwell, 101 Cal. 553; 36 Pac. R. 107 (1894).

[2] *Supra*, p. 126.

[3] Especially Preston *v.* Fitch, 137 N. Y. 41 (1893).

[4] Patton *v.* Carr, 117 N. C. 176; 23 S. E. 182 (1895); Burdick's Cases on Part. 248.

(a) *Judgments against the Surviving Partner.*— Equity will subordinate the lien upon firm property of judgments, obtained by separate creditors against the survivor, to partnership liabilities. Such creditors will be limited to the share of their debtor; and that share, as we have seen, is only his interest in the balance which remains after the firm debts and the equities of partners are satisfied. If, then, the surviving partner is indebted to the firm, that debt must be paid out of firm property, before a court of equity will permit the separate judgment creditors to enforce their judgments against the firm assets in the hands of the surviving partner. Nor does it matter that judgments are obtained and executions levied before the representative of the deceased partner institutes proceedings in equity.[1] Survivorship does not work a merger of the firm title in the individual title, at least in equity.

The same doctrine has been enforced by common law courts. Upon the death of a partner and the levy of an execution by a firm creditor on the firm assets, the two surviving partners claimed their personal property exemptions out of the firm effects. By the law of that jurisdiction a partner is entitled to this exemption, if his copartners consent. Each of the survivors assented to the other's claim of exemption, insisting that the representative of the deceased partner had no voice in the matter. But the court refused to take this view, saying that to sustain their contention "would be 'to stick in the bark' and to abandon the principle upon which the rule has been established; that although the partnership was dissolved by the death of A. J. Boyd, still his estate (his administrator) has the same interest in its effects and is

[1] Maddock's Admx. *v.* Skinner, 93 Va. 479; 25 S. E. 535 (1896); Burdick's Cases on Part. 250.

under the same obligation to its creditors that A. J. Boyd was when living."[1]

(*b*) *Bankruptcy of Surviving Partner.* — That the firm title to firm property is not merged in the individual title of the surviving partner has been repeatedly adjudicated in bankruptcy cases. Dawson and Windross had been partners. Dawson died; Windross deposited firm moneys with third parties for the payment of firm creditors, and became bankrupt. Yet these moneys were held to be firm assets, and not a part of Windross's separate estate.[2]

4. By Partnership Agreement a Deceased Partner's Interest may vest in his Representative. — While the death of a partner ordinarily dissolves the firm and vests the partnership title in the survivors, this result may be prevented by the agreement of the partners. If they stipulate that, in case of the death of a member, "his or her legal heirs or legal representatives shall occupy the same place in the copartnership as was occupied by the partner," such death does not dissolve the firm, nor in any way change the relations of the survivors to the firm title.[3] The partnership continues without a break, the representative of the deceased member taking his place as in a joint stock company.

5. By Partnership Agreement, a Deceased Partner's Interest may vest in the Survivors. — On the other hand, the partners may agree that upon the death of any of their number, the survivors shall become the absolute owners of the firm assets, with a personal liability to pay the

[1] Richardson *v.* Redd, 118 N. C. 677; 24 S. E. 420 (1896); Burdick's Cases on Part. 260.

[2] Ex parte Leaf, In re Simpson & Windross, 4 Deac. 287 (1840). See Ex parte Manchester Bank, In re Mellor, 12 Ch. D. 917 (1879); Burdick's Cases on Part. 263; and U. S. Bankruptcy Law of 1898, § 5 (a).

[3] Rand *v.* Wright, 141 Ind. 226; 39 N. E. 447 (1895); Burdick's Cases on Part. 266.

deceased partner's representatives for his interest. If the firm is solvent, such an agreement operates to convert the title of the original firm instantly upon the death of a member into the title of the survivors. If the agreement provides that the death shall not dissolve the firm, but that the survivors shall carry on the business, it relieves the survivors from the necessity of winding up the affairs of the old firm and constitutes them partners in a new firm; but it does not secure the continuance of the old firm title, either for the benefit of the deceased partner's representatives or for the benefit of the old firm's creditors. The right of the representatives is to have the value of their testator's interest ascertained in the method prescribed by the agreement, and paid by the survivors in the stipulated manner. They cannot insist upon having the old firm assets applied to the payment of its debts; nor can its creditors, upon the bankruptcy of the survivors, compel the appropriation of any assets of the old firm, remaining *in specie*, to the satisfaction of their claims, in preference to the claims of creditors of the new firm.[1]

(*a*) *Such an Agreement must be explicit.* — Provisions which extinguish the right of an outgoing partner to have the firm assets applied to the payment of firm debts, whether operating against[2] or in favor[3] of the estate of the deceased partner, or when they are contained in dissolution agreements between living partners,[4] are strictly construed. Their language must show clearly and explicitly that the parties intended to destroy the right.

[1] In re Simpson, 9 Ch. App. 572 (1872).

[2] In re Simpson, *supra*.

[3] Ex parte Morley, 8 Ch. App. 1026 (1873).

[4] In re Daniel, Ex parte Powell, 3 Manson's Bankruptcy R. 312; 75 L. T. 143 (1896). "Generally speaking, the equitable right of the outgoing partner will continue unless there are clear words taking it away."

Such provisions are looked upon as "very special"[1] and exceptional.

In Ex parte Morley, the partnership agreement provided that, upon the death of W. White, the shares of his copartners, W. T. White, his son, and Collins, should belong to W. White's personal representatives, who should pay to these survivors sums equal to their shares of the profits during the preceding year, and £500 in addition. Yet the court held that it was not intended by the deed to alter the rights of creditors, and vest the entire assets in the father's representatives, but to vest them in such representatives subject to the payment of the debts. Lord Justice James said: "There was nothing in that deed, if it could have been valid as against the rights of creditors, which professed to say that the son or the other partners going out were not to have their usual legal inherent right to be indemnified against the debts, in the mode in which the court of bankruptcy or the court of chancery indemnifies a person in respect of debts to which he is liable, but from which he is entitled to be exonerated by some one else. The mode in which that sort of thing is done is this: that, if there be two estates, a joint estate and separate estate, the court takes care that the joint assets are applied in payment of the debts of the joint creditors, before any part of them goes to the separate creditors. The trade assets, beyond all question, were joint assets, so far as they remained *in specie*. Those, therefore, were to be applied in payment of the joint creditors, so far as there were any joint creditors remaining, and, if there was a surplus, that would be applied among the persons entitled to it."

The decision has been followed in England without question. In a later case the partnership agreement between a father and son provided that the machinery and

[1] Ex parte Dear, 1 Ch. D. 514 (1876).

stock in trade should belong to the father, and not form part of the capital of the firm. Yet the court held that this machinery and stock were firm assets; that upon the father's death, the son had the right to have every shilling of this joint estate applied in payment of the joint debts; and that joint creditors had the right to have this estate, so far as it remained *in specie*, upon the son's bankruptcy appropriated to the satisfaction of their claims.[1]

### § 5. Liability of Surviving Partners.

In the preceding section, the liability of the surviving partner to the estate of his deceased associate has been stated in general terms. It will be referred to again in Chapters VI. and VIII.

His liability to the creditors of the firm is not confined to an honest and faithful disposition of its assets and to their application to the firm debts. He is personally liable for every obligation of the partnership; and actions for the enforcement of such obligations are to be brought against him alone. Even though the action is an equitable one and calls for an accounting, if it has for its object the collection of a partnership indebtedness, it is properly brought against the survivor alone. The representatives of the deceased partner are strangers to the obligation.[2] They are not to be joined as defendants with the surviving partner;[3] although the estate of the deceased partner may be compelled, by appropriate proceedings against it, to pay partnership debts. The nature of

[1] Ex parte Manchester Bank, In re Mellor, 12 Ch. D. 917 (1879); Burdick's Cases on Part. 263.

[2] Rusling *v.* Brodhead, 55 N. J. Eq. 200; 35 At. 841 (1896); Burdick's Cases on Part. 273.

[3] "A surviving partner is the representative of his house; in him their rights concentre, and from him their dues are to be exacted; if only one remain, he may be sued alone without joining the executors of his companions." Lex Merc. Am. 446, 447.

such proceedings will be discussed in the last section of Chapter V.

1. SURVIVING PARTNER AS A SURETY FOR THE FIRM. — While the surviving partner is liable to be sued alone by firm creditors, because of the joint character of all firm obligations, yet, whenever he is obliged to satisfy them out of his individual property, he acts as surety for the firm, and not as a principal common law joint obligor. If he borrows money with which to meet them, he may apply the proceeds of firm property to the repayment of the loans.[1] In case he makes an assignment for the benefit of creditors, before repayment, he may include the loans in the list of firm debts which are to be paid by the assignee out of firm assets.[2] If the property of the firm is insufficient for the payment of its debts, the surviving partner, upon discharging them, is entitled to contribution from the estate of the dead partner as a co-surety for the firm.[3]

## § 6. Firm Debts and Partners' Joint Debts.

If it is true that a "partnership as such has its own property, and its own creditors, as distinct from the individual property of its members and their individual creditors,"[4] it should follow that a judgment against the members of a partnership, for an indebtedness not con-

[1] Kenney *v.* Howard, 68 Vt. 172; 34 At. 700 (1896); Burdick's Cases on Part. 271. The surviving partner in this case gave a bond to apply the proceeds of the sales of firm property "on said indebtedness of the firm." Pending the sale of the property he borrowed money for the payment of firm debts, giving his individual notes therefor. The court held that in applying the proceeds of subsequent sales of firm property to the satisfaction of these notes, the survivor was applying them "on said indebtedness of the firm."

[2] Durant *v.* Pierson, 124 N. Y. 444; 26 N. E. 1095 (1891).

[3] See Chap. VI., § 3, *infra*.

[4] Bulger *v.* Rosa, 119 N. Y. 459, 467; 24 S. E. 853 (1890).

nected with firm affairs, is not enforceable against the firm's property. Under it only the separate property of the partners and their several shares in the firm assets can be sold.[1] Nor should it matter that the judgment is obtained upon a joint obligation of the partners.[2] This view is supported by no little judicial authority.[3]

1. No Distinction between Firm Debts and Partners' Joint Debts in some Jurisdictions. — In England, all joint obligations of the partners are collectible out of partnership assets, whether contracted in the business of the firm or outside of it. Accordingly, if the members of a firm together with others enter into a joint and several bond, the obligee may sue the partners as joint promisors, and upon recovering judgment may take out execution against the partnership assets, although the bond has no connection with the partnership business; or if the firm is in bankruptcy, he may prove against the firm estate.[4]

(a) *Reasons assigned by American Courts.* — The courts in this country which have permitted judgments against partners upon their joint obligations unconnected with the partnership business, to be collected out of firm assets, have based their decisions on the following grounds.

Firm creditors, it is said, can enforce their claims against the firm property only through the equity which the members of the firm possess to have the firm property applied to firm assets. This equity the partners surrender when they enter into a joint obligation, for they thereby clothe the obligee with authority to take joint property in satis-

[1] Richards *v.* Le Veille, 44 Neb. 38; 62 N. W. 304 (1895); Burdick's Cases on Part. 281.

[2] Whelan *v.* Shain, 115 Cal. 326; 47 Pac. 57 (1896); Burdick's Cases on Part. 283.

[3] In re Holbrook, 2 Low. (U. S.) 259 (1873); Ex parte Weston, 12 Met. (53 Mass.) 1 (1846); Dunica *v.* Clinkscales, 73 Mo. 500 (1881); Wall *v.* Fife, 37 Pa. 394 (1860).

[4] Hoare *v.* Oriental Bank Corp., 2 App. Cas. 589, 597 (1877).

faction of the joint debt. The joint debt, being the debt of each partner, neither has any equitable right to insist that firm assets should be applied to the firm debts rather than to this debt.[1]

This reasoning, it will be seen, ignores the doctrine that "firm creditors are preferentially entitled to be paid out of the firm assets," and that this equity is an "element in the security of the firm creditors"; [2] or, in other words, that this equity is a property right of the creditors. In Saunders *v.* Reilly, it is said that the partners, although insolvent, could have taken their firm property and applied it upon a joint judgment, which was not obtained upon a firm debt. But no authority is cited for this important proposition, a proposition which, it is submitted, is unsound in principle, and opposed to the weight of authority. Moreover, it appears to be irreconcilable with the doctrines which have been repeatedly affirmed by the court which announced it.[3]

(*b*) *Claims of Joint Creditors in Bankruptcy.*— Whether, upon the bankruptcy of a partnership, creditors, holding the joint obligations of the partners unconnected with the firm business, can share *pari passu* with the firm creditors in firm assets, appears to depend upon the provisions of the bankruptcy statutes.

In England, as we have seen, no distinction is made between these two classes of debts. The language of the statute is as follows: "In the case of partners the joint estate shall be applicable in the first instance in payment of their joint debts, and the separate estate of each partner

[1] Couchman *v.* Maupin, 78 Ky. 33 (1879); Saunders *v.* Reilly, 105 N. Y. 12; 12 N. E. 170 (1887); Burdick's Cases on Part. 277.

[2] Bulger *v.* Rosa, 119 N. Y. 459; 24 S. E. 853 (1890).

[3] See Menagh *v.* Whitwell, 52 N. Y. 146 (1873); Burdick's Cases on Part. 222; Bulger *v.* Rosa, *supra*, and other New York cases referred to in the preceding section.

shall be applicable in the first instance in payment of his separate debts."[1] Hence the courts recognize but three classes of creditors, in administering the estates of bankrupt partners: first, creditors to whom all the partners are jointly liable; second, creditors to whom the partners are liable severally and respectively; third, creditors to whom the partners are liable both jointly and separately for the same debt.[2]

Moreover, the English statute permits the consolidation of bankruptcy proceedings against joint debtors. Under this provision, the courts have consolidated the separate adjudications of two firms, having the same members, and have distributed their aggregate properties as one estate.[3] This course appears to have been followed by a Federal District Court in one instance.[4] The facts are meagrely set forth, but according to the statement in the report, the bankrupt partners had succeeded to the business of one partnership in New York, and to that of an entirely distinct one in Philadelphia. Nor is there any intimation that they had merged the two sets of capital, or consolidated the two business houses. Yet the court declared that they ought not to be treated as separate and distinct firms in the distribution of assets belonging to the bankrupts.

As a rule, however, our courts, in administering bankrupt estates, have treated the firm creditors as preferentially entitled to the firm assets. In Re Nims,[5] the subject is discussed at length by Judge Blatchford, and the con-

[1] British Bankruptcy Act of 1883, § 40 (3).

[2] Lindley on Part. (5th ed.), *701.

[3] Harris v. Farwell, 13 Beav. 403 (1846).

[4] In re Vetterlein, 5 Ben. (U. S. Dist. Ct.) 311 (1871); Burdick's Cases on Part. 276.

[5] 16 Blatch. (U. S. Cir. Ct.) 439 (1879), reversing the decision of the District Court, which is reported in 18 N. B. R. 91 (1878), to the effect that "joint creditors share equally in joint assets, whether their debts are partnership debts or not."

clusion is reached that "debts of the firm are different in character from other joint debts of the partners."

## § 6. (A.) Firm Debt is a Debt of Each Partner.

While a partnership has its creditors as distinct from the separate creditors of its members, it does not follow that firm creditors are not also creditors of the several partners. Unless a partnership is changed into an artificial person by statute, contracts entered into in its name are the contracts of its members.[1] They are personally liable to the extent of their several fortunes for all firm obligations. Therefore, in determining whether an insolvent's indebtedness amounts to the sum required by statute to be owing to the petitioning creditors, a promissory note, given to such creditors by a firm of which the debtor was a member, is to be treated as his debt.[2]

1. A Partner may pay Firm Debts with his Separate Property. — We have seen that the use of firm property by the partners for the payment of their separate debts is a fraud upon the firm creditors. But a partner does not hinder, delay, or defraud his separate creditors by applying his separate estate to the satisfaction of firm debts. The owners of such debts, upon obtaining judgment against the firm, could levy upon the property of each partner, and sell it,[3] while the judgment creditor of a partner under a levy upon partnership property can sell only his debtor's share. As the firm creditors can thus

[1] *Supra*, Chap. III. § 1. But see Hornblower, J., in Curtis *v.* Hollingshead, 2 Green (N. J. L.), 402 (1834); Burdick's Cases on Part. 285.

[2] Hinds *v.* Heath (N. H.), 38 At. 382 (1896). The statute of New Hampshire further provides that "the insolvency of a partnership shall render each partner insolvent within the meaning of this chapter," &c. See Schmidt *v.* Ellis, 38 At. 382 (1897).

[3] This topic will be more fully discussed in Chap. V. § 1, *infra*.

compel the application of the separate property of a partner to the satisfaction of their claims, he may lawfully transfer it to them in payment.[1]

2. THE MERCANTILE VIEW OF FIRM DEBTS. — While the legal doctrine, that the debts of a firm are the debts of each of its members, is well established, merchants look upon the firm as the debtor. "In ordinary commercial language the obligation of a firm would not be spoken of as the obligation of any one of its members, and a firm is regarded as an entity distinguished from all the individual members of which it is composed." [2]

How, then, should a contract of mortgage or pledge be construed, in which a member of a firm agrees that certain of his individual property may be applied by the other contracting party to the payment of all sums of money which may be owing upon any account whatever by the first party to the second party? In the case last cited, the New York Court of Appeals declared that such a contract "must be regarded as a commercial instrument, executed in commercial transactions, and must be construed as ordinary commercial men would understand the language used"; that, as among business men, a distinction is made between the firm as an entity, and the members who compose it, the language of the contract would not be understood by them as broad enough to cover the indebtedness of a firm of which the mortgagor was a member, "and for whose debts, jointly with the other members of the firm, he could be made responsible."

[1] Newman *v.* Bagley, 16 Pick. (Mass.) 570 (1835); Burdick's Cases on Part. 285.

[2] Bank of Buffalo *v.* Thompson, 121 N. Y. 280 (1890); Burdick's Cases on Part. 286; *cf.* Succession of Pilcher, 39 La. Ann. 362; 1 So. 929 (1887), holding that the statute, giving to a minor heir $1,000, in preference to her ancestor's creditors, did not apply to his share in a partnership, as the firm debts were not contracted by him as an individual, but by the firm.

(*a*) *Mercantile View Discredited in Massachusetts.* — On the other hand, the Supreme Court of Massachusetts has given a very different construction to language which was substantially the same.[1] Mr. Justice Holmes, speaking for the majority of the court, said: "The clause pledging the property for any other claim against the debtor is not inserted with a view to certain specific debts, but as a drag-net to make sure that whatever comes to the creditor's hands shall be held by the latter until its claims are satisfied. Corey on Accounts and Lindley on Partnership have made it popular to refer to a mercantile distinction between the firm and its members. But we have no doubt that our merchants are perfectly aware that claims against their firms are claims against them; and when a merchant gives security for any claim against him, and there is nothing to cut down the literal meaning of the words, he must be taken to include claims against him as a partner."

### § 6. (B.) Sole Debt of a Partner for Firm Benefit.

A person who lends money or sells property to a partner, upon his credit, becomes his separate creditor. Nor will he be transformed into a creditor of the firm, by the fact that the money or property was acquired by his debtor for the benefit of the firm.[2] Its transfer to the partnership

[1] Hallowell *v.* Blackstone Nat. Bank, 154 Mass. 359; 28 N. E. 281 (1891); Burdick's Cases on Part. 288. The clause in question read: "It is hereby agreed that such surplus, or any excess of collaterals upon this note, shall be applicable to any other note or claim against me held by said bank." The note, which was accompanied by these collaterals and this contract, was the individual note of the pledgor.

[2] Barton *v.* Hanson, 2 Taunt. 49; 2 Camp. 97 (1809). In this case, partners in a coach line divided the road into sections, each providing the horses for his district. Plaintiff, with knowledge of this arrangement, sold feed to one of the proprietors for his horses, and stabled them, taking in part payment a bill accepted by him individually. The court held that the debt was that of the individual proprietor and not of the firm.

by his debtor has no more effect on his relations to the debtor than its transfer to a stranger would have had.

It often happens, however, that a transaction which assumes the form of a personal contract between a third person and a partner, is in fact a contract between the third person and the firm. Such person is a firm creditor, although he may be also a separate creditor of the contracting partner. In an early case, in which one partner borrowed money for the use of the firm, giving therefor his note, and later his bond, Lord Chancellor Hardwicke observed: "It is very true there might have been a loan to the partnership, notwithstanding the notes were given by one of them only; and if the contract had been originally between the petitioner and both the partners, though the bond is executed by one only, yet it would be considered as a collateral security, and both of them would have been liable notwithstanding."[1]

(a) *A Difficult Question of Fact.* — Whether the transaction gives the creditor a claim upon the firm, as well as upon the contracting partner, is sometimes a difficult question of fact. This is well illustrated by two English cases tried before Lord Ellenborough. In the earlier case, E. L. Lye, who was in partnership with Geo. Lye, under the firm name of Geo. Lye & Son, drew bills of exchange in his individual name, which were discounted by a banker, and the proceeds were used by the firm. Plaintiffs, as assignees in bankruptcy of the banker, sought to recover against the firm on the ground that the transaction was a loan of money to the firm. "But," said Lord Ellenborough, "the bills, considering the transaction as a discount between the parties, are his only. But it is contended that, as the proceeds went to the use of the partnership, the partners are therefore liable upon the other counts. I am at a loss to discover what difference that circumstance can

[1] Ex parte Hunter, 1 Atkyns, 357 (1742).

make, if it were originally a mere matter of discount; and I do not find any evidence to show that it was anything else. It was supposed indeed by Burrough (the bankrupt) that the money would be applied to the partnership use; and to such use it was in fact applied; but nothing passed from the defendants to induce him to believe that it was a partnership concern, and to lend his money on that account. It does not appear that any contract of that sort took place, nor anything more than the mere discount of the bills; and it would be highly dangerous to follow the proceeds into the hands of every party to whose use they may be applied."[1]

In the later case, one member of an English firm, who was the manager of its business in New York, drew bills on the firm, payable to plaintiffs' order, and upon them raised money from plaintiffs for the use of the firm. This was done with the knowledge and approval of all the partners. Lord Ellenborough considered this case distinguishable from Emly *v.* Lye, declaring that the transaction was a loan rather than a discount, and that the bills were given as security for the money borrowed from the plaintiffs. The fact that the house in England had regularly accepted and paid bills of this character, until its bankruptcy, indicated that all parties understood the transaction to be that of a loan to the firm, and not of a purchase of the drawing partner's bill.[2]

The soundness of the doctrine announced in these two cases, as well as the difficulty in applying it, is recognized by the American courts.[3]

1. Negotiable Paper in the Name of a Partner may be a Firm Contract. — We have seen, in a previous

[1] Emly *v.* Lye, 15 East, 7 (1812).

[2] Denton *v.* Rodie, 3 Camp. 493 (1813).

[3] Logan *v.* Bond, 13 Ga. 192 (1853); Bonnell *v.* Chamberlain, 26 Conn. 487 (1857); Maffet *v.* Lenckel, 93 Pa. 468 (1880).

section,[1] that a note or bill, in the name of one partner, is the contract of the firm whenever the partner's name is adopted or held out as the firm name. In such cases, the paper is not collateral security for the firm debt, but represents the debt itself, and all the partners may be sued upon it.

2. THE DEED OF A PARTNER. — A partnership creditor may, as Lord Hardwicke pointed out, take a bond from one partner as collateral security for the debt. He may also take the bond in conditional payment of the firm debt, without losing his claim against the firm in case the bond is not paid.[2] When, however, an instrument under seal is executed and delivered by one partner, upon his receiving money or property from the obligee, the latter can rarely claim to be a firm creditor. In the absence of fraud or mistake, the courts will treat him as having intended to take the partner for his sole debtor.[3] Accordingly, a person who conveys land to one partner, and receives from him in part payment of the purchase price his bond and mortgage, has no claim against the firm for the unpaid purchase money. The only one liable to him therefor is the obligor in the bond.[4]

(*a*) *Unauthorized Deed in Firm Name.* — In what cases one partner may bind the firm by an instrument under seal in the firm name, will be considered in the next chapter. Our present inquiry is directed to the rights of a firm creditor, who has received such an instrument for a firm debt, from a partner who executed and delivered it without authority from his associates.

That the instrument is effective,[5] against the executing

[1] *Supra*, Chap. III. § 1.

[2] Wallace *v.* Fairman, 4 Watts (Pa.), 378 (1835).

[3] Patterson *v.* Brewster, 4 Edw. Ch. (N. Y.) 352 (1844).

[4] Williams *v.* Gillie, 75 N. Y. 197 (1878); Burdick's Cases on Part. 290.

[5] A few courts have taken the view that the executing partner

partner, as his deed, follows from the principles set forth in the first section of this chapter. The firm name is equivalent to the names of each partner. But has the obligee destroyed his claim against the firm by receiving this deed which is the specialty contract of one partner only? The answers given by the courts are not entirely harmonious.

(*b*) *When Seal is Surplusage.* — In some jurisdictions, an unauthorized seal to a partnership contract is treated as surplusage, whenever it is unnecessary to the validity of the transaction.[1] Other courts have refused to take this view, and have held that the instrument is not to be treated as the specialty of the firm because the seal was unauthorized by its members, nor as the simple contract of the firm, because it was not intended by the partner delivering and the obligee receiving it as a simple contract. They intended to enter into a specialty contract, some of the characteristics of which are radically different from those of a simple contract.[2]

(*c*) *Partnership Contract not merged in an Unauthorized Specialty.* — Another view is that when a partner, without authority from the firm, puts the contract, between the firm and the third person, into the form of a specialty, the firm obligation is not merged therein. Nor is the seal a surplusage. The deed may be available against the executing partner; but the third person has the right to hold the firm to a simple contract obligation, whose terms are evidenced by the sealed writing.[3]

cannot be sued alone on such a deed, because it was not delivered as his individual deed, but that of the firm. Fisher *v.* Pender, 7 Jones L. (N. C.) 483 (1860); Hart *v.* Withers, 1 P. & W. (Pa.) 285 (1830).

[1] Cook *v.* Gray, 133 Mass. 106 (1881); Moore *v.* Stevens, 60 Miss. 809, 816 (1883); same principle in Blanchard *v.* Blackstone, 102 Mass. 343 (1869); Worrall *v.* Munn, 5 N. Y. 229 (1851).

[2] Russell *v.* Annable, 109 Mass. 72 (1871); Schmetz *v.* Shreeve, 62 Pa. 457 (1869); same principle, Wheeler *v.* Nevins, 34 Me. 54 (1852).

[3] Walsh *v.* Lennon, 98 Ill. 27 (1881); Brown *v.* Bostian, 6 Jones

In Walsh *v.* Lennon, plaintiff, upon lending money to a firm, received a promissory note signed in the names of the partners by one of them, who also attached seals. The court said: "It is undoubtedly true, that one partner has no power to bind the firm by deed, but this instrument is not sued upon as a deed. The declaration contains the common counts. The proof shows defendants were partners, and that the writing in question has the firm name attached thereto by one of the partners. This partner had the right to borrow money on the credit of the firm, and give the promise of the firm for its payment. A seal is not necessary to render such a promise effective. The writing, without reference to its effect as an obligation, contains a written admission that the money was borrowed by the firm at the agreed rate of interest mentioned."

(*d*) *Rights of Surety upon an Unauthorized Firm Deed.* — One who signs, as a surety, a specialty of the character we have been considering, has no rights against the firm on the instrument. He is not entitled, therefore, to be subrogated to any claims of the obligee against the firm. His rights of subrogation are limited to the obligee's claims against the executing partner. But in case this partner had the implied power to bind the firm upon a contract of indemnity, the surety can enforce such contract against the partnership.[1]

### § 6. (C.) Firm Debt Converted into Separate Debt.

The members of a partnership cannot convert a firm debt into the separate debt of one of their members, without a contract to that effect with the creditor. According-

L. (N. C.) 1 (1858); Hoskinson *v.* Eliot, 62 Pa. St. 393 (1869); same principle, Osborne *v.* High Shoals Co. 5 Jones L. (N. C.) 177 (1857); Hermanos *v.* Duvigneaud, 10 L. Ann. 114 (1855).

[1] Wharton *v.* Woodburn, 4 Dev. & B. L. (N. C.) 507 (1839); Durant *v.* Rogers, 87 Ill. 508 (1877).

ingly, if a firm is dissolved, and its members agree that one shall take the assets in consideration of his assuming and paying its debts, this agreement does not discharge the retiring partners from liability to firm creditors. Nor will they be discharged by the mere assent of a creditor unless the transaction amounts to a novation.[1] What constitutes a novation will be discussed hereafter.[2]

1. Retiring Partner as a Surety. — In case of a contract between the partners that one shall pay the firm debts, upon taking the firm assets, the relation of principal and surety is created between the purchasing and selling partners.[3] If the latter is compelled to pay firm debts out of his own property, he is entitled to be reimbursed by the former. As between themselves, the selling partner becomes a separate creditor of the purchasing partner, upon discharging firm debts.[4]

Whether, by a contract of this kind and notice to creditors, the liability of the retiring partner to them is at all changed, is a question upon which the authorities are divided.

(*a*) *Creditors Must Assent to the Change of Relation.* — On the one hand it is maintained that the rights of creditors against the partners with whom they contracted rest upon the terms of the contract, which cannot be varied without the consent of the creditors. "It requires the same mutuality to vary or modify a contract," the advocates of this view declare, "as it does to create it in the first instance. The modification is only a species of contract."[5]

[1] Motley *v.* Wickoff (Mich.), 71 N. W. 520 (1897); Burdick's Cases on Part. 293.

[2] *Infra*, Chap. V. § 1.

[3] Rodgers *v.* Maw, 15 M. & W. 444; 4 Dow. & L. 66 (1846).

[4] Ex parte Carpenter, Mont. & McAr. 1 (1826); Wood *v.* Dodgson, 2 M. & S. 195 (1813); Moody *v.* King, 2 B. & C. 558 (1824).

[5] Hall *v.* Jones, 56 Ala. 493 (1876).

"This doctrine," in the opinion of the Supreme Court of Texas, "that a contract, when once made, cannot be unmade without consent of both parties thereto, is so evidently sound, just, and correct that no argument is required to sustain it."[1]

Even where this doctrine prevails, a creditor who has received, from the original firm, ample securities for his claim, will discharge the retiring partner by surrendering them to the new firm. Not on the ground, it is said, that the retiring partner is but a surety for the new firm, but for the reason that such a surrender is an appropriation by the creditor of assets of the old firm, sufficient to pay the debt.[2]

(*b*) *Notice to Creditors is Sufficient.* — The weight of authority in this country, however, is opposed to the doctrine stated in the foregoing paragraph. According to the prevailing view, the right of the retiring partner to be treated as a surety, within limits presently to be pointed out, rests upon equitable principles, and not on any contract between him and the creditors.[3]

The retiring partner does not cease to be a principal debtor when he becomes a quasi surety. By notifying the creditor of the agreement between himself and those who have assumed the firm debts, he cannot compel the creditor to sue them. The creditor's right to proceed at law against all the members of the old firm is unaffected by such a notice.[4] Moreover, if he is not informed of the agreement between the partners, he may take the notes of the continuing partners or of a new firm, for the debt of

[1] Shapleigh Hardware Co. *v.* Wells, 90 Tex. 110; 37 S. W. 411 (1896).

[2] First Nat. Bank *v.* Cheney, 112 Ala. 536; 21 So. 1003 (1896).

[3] Brandt on Suretyship (2d ed.), § 32.

[4] Bazille *v.* Board of Commissioners of Ramsey County, 73 N. W. (Minn.) 845 (1898).

the old one, especially if he reserves his rights against the retiring partner, without discharging the latter.[1]

But if the creditor does not enforce his claims against all the members of the old firm, any dealings between him and the continuing partners or the new firm, after notice of the agreement, which would discharge an ordinary surety, will discharge the retiring partners.

(c) *Illustrations of the Prevailing Doctrine.*—This is well illustrated by a decision of the New York Court of Appeals.[2] Tallman & Barnes, upon dissolution of their partnership, agreed that Tallman should transfer his interest to Barnes, and that the latter should pay all the firm debts. Notice of this agreement was given by Tallman to the plaintiff, who held an overdue note of the firm. He also requested the plaintiff to collect the note from Barnes without delay; but plaintiff did not institute proceedings for its collection until after Barnes's insolvency, and the court held that, by his failure to collect the note from Barnes during the latter's solvency, the plaintiff had discharged Tallman.

According to the doctrine which we are now considering, the retiring partner is discharged by a valid agreement between the assuming partner and the creditor, extending the time of payment,[3] or voluntarily compromising the debt,[4] or releasing securities held by the creditor.[5]

2. Fluctuating Views in England.—The doctrine which, as we have seen, is the prevailing one in this country, was based on a dictum in a House of Lords

[1] Palmer *v.* Purdy, 83 N. Y. 144 (1880).

[2] Colgrove *v.* Tallman, 67 N. Y. 95 (1876).

[3] Miller *v.* Thorn, 56 N. Y. 402 (1874); Fernald *v.* Clark, 84 Me. 234; 24 At. 823 (1892).

[4] Mathews *v.* Colburn, 1 Strob. L. (S. C.) 258 (1847).

[5] Bell *v.* Hall, 5 N. J. Eq. 477 (1846).

decision.[1] But the declaration of Lord Lyndhurst in that case, that a retiring partner becomes a surety for a new firm which assumes the old firm's debts, by giving notice to creditors of his contract with the new firm, was soon criticised,[2] and, after having been treated by the courts as a mere dictum,[3] was apparently nullified by the Partnership Act. This declares that "a partner who retires from a firm does not thereby cease to be liable for partnership debts or obligations incurred before his retirement. A retiring partner may be discharged from any existing liabilities by an agreement to that effect between himself and the members of the firm as newly constituted and the creditors, and this agreement may be either express or inferred as a fact from the course of dealing between the creditors and the firm as newly constituted."[4]

The doctrine has been reinstated, however, by a recent decision of the House of Lords.[5]

### § 7. The Nature of Firm Contracts.

Frequent references have been made in the preceding sections of this chapter, to the opposing views which are entertained concerning the nature of partnership contracts. According to one view there is, in law, no such thing as a firm contract. In the language of a learned author: "Every joint contract is an aggregate of the

1 Oakelley *v.* Pasheller, 4 Cl. & F. 207 ; 10 Bligh, N. S. 548 (1836).

2 "This quasi suretyship is surely a false analogy, unless the creditor has assented to such a change in his debtor's position." Lind. on Part. (5th ed.) *252, note *x*; (6th ed.) 258, note *z*; Oakford *v.* Eur. & Am. Co. 1 Hen. & Mil. 182 (1863) ; also opinion of Lindley, L. J., in Rouse *v.* Bradford Banking Co. [1894] 2 Ch. 32, 58–60.

3 Swire *v.* Redman, 1 Q. B. D. 536 (1876) ; Cockburn, C. J., pointed out that in Oakelley *v.* Pasheller, the creditor had assented to the substitution of debtors.

4 British Part. Act of 1890, § 17 (2) & (3).

5 Rouse *v.* Bradford Banking Co. [1894] A. C. 586. See criticism of this case in De Colyar's Law of Guaranty (3d ed.), 317, 318.

several contracts of the partners. The fact is, that the jointness of the contract is nothing but a form. The only contracts that have a substantive existence, are the individual contracts of the partners." [1]

1. Effect of a Partner's Death on a Contract with an Employee. — Where this view prevails, it is held that the death of a partner, although dissolving the firm, does not, as a matter of law, dissolve a contract for personal services to the firm.[2] In the last cited case, the court declared that the common law does not know the firm as an entity; that a contract with a firm is a contract with the members who compose it; and that where the death of a partner would not naturally put an end to the business, and the business in fact is continued by the survivor, the latter is bound to carry out the contract with the employee, as he would be bound to complete a firm contract for the erection of a building.

In jurisdictions, however, where the firm is deemed a contracting party, as distinct from its individual members, the death of a partner in a firm of employers dissolves a contract for personal services, whenever an individual employer's death would have that result. Such a contract has "reference to a certain existing partnership business only. Any business carried on after the death of one partner might be a totally different one." [3]

If the firm is an employee or agent instead of an employer, the death of a partner certainly ought to dissolve the contract.[4]

2. Option to Treat the Contract as Dissolved. — Even if the true conception of a firm contract were that

[1] Parsons (James), Principles of Part. (1st ed.) §§ 95, 96.

[2] Hughes *v.* Gross, 166 Mass. 61; 43 N. E. 1031 (1896); Burdick's Cases on Part. 296.

[3] Tasker *v.* Shepherd, 6 H. & N. 575, 581 (1861).

[4] Friend *v.* Young [1897], 2 Ch. 421, 429.

it is merely a bundle of its members' several contracts, the other contracting party should be accorded the option of treating it as dissolved by a change in the membership of the firm, whenever the personality of its members is a material element in the contract relation.

If one becomes a surety to a firm, he has a surety's right to stand upon the very terms of his contract. To hold him liable as surety to a different association of persons would be to make a new contract for him. Hence the death or retirement of a partner[1] or the introduction of a new member[2] into the firm discharges the surety from future liability.

In Strange *v.* Lee, the defendant became surety for Blyth to the banking house of Wallwyn, Savage & Co. for the payment of all sums advanced by the partners to Blyth. After Wallwyn's death, the survivors continued to advance money to Blyth, and upon his default sued Lee on the bond; but the court held that the defendant contracted as surety to the partnership as constituted at the time of his engagement, and not to the banking house, "however the individual partners might change." Said Lord Ellenborough, "It may make a very material difference in the view of the obligor, as to the persons constituting the house at the time of entering into the obligation, and by whom the advances are to be made to the party for whom he is surety: for a man may very well agree to make good such advances, knowing that one of the partners, on whose prudence he relies, will not agree to advance money improvidently. The characters, therefore, of the several partners may form a material ingredient in the judgment of the obligor upon entering into such an engagement."

[1] Strange *v.* Lee, 3 East, 484 (1803).

[2] Barnes *v.* Barrow, 61 N. Y. 39 (1875); London & L. Ins. Co. *v.* Holt, 10 S. D. 171; 72 N. W. 403 (1897).

(*a*) *Contract may be for Suretyship to a Fluctuating Firm.* — If the terms of the contract[1] or the circumstances of the case[2] justify such a construction, the obligor may be held liable as surety to a partnership, however shifting its membership may be, or to its surviving members.

Moreover, the secret withdrawal of a partner will not necessarily terminate the suretyship. If a person gives a mortgage to a firm, to secure it for indorsements of his paper, the mortgage will remain a valid security for such indorsements in the old firm name, after the secret withdrawal of a partner.[3]

These principles apply, also, to contracts of suretyship for a firm.[4]

(*b*) *Other Instances of Dissoluble Contracts.* — If the contract stipulates for the personal services of a particular partner, his death will justify the other contracting party in treating the contract as dissolved.[5] One apprenticed to a firm has a right to insist that he shall be instructed in the trade by the members then composing it.[6] A client is discharged from his contract with a firm of lawyers, upon a dissolution of the partnership,[7] unless they remain jointly engaged in his service and jointly responsible to him for any mistake or negligence by either in the performance of the contract.[8]

[1] Nat. Bk. of Newburg *v.* Bigler, 83 N. Y. 51 (1880).

[2] Metcalf *v.* Bruin, 12 East, 400 ; 2 Camp. 422 (1810).

[3] Buffalo City Bank *v.* Howard, 35 N. Y. 500 (1866).

[4] The British Partnership Act, § 18, declares : "A continuing guaranty or continuing obligation given either to a firm or to a third person in respect of the transactions of a firm is, in the absence of agreement to the contrary, revoked as to future transactions by any change in the constitution of the firm to which, or of the firm in respect of the transactions of which, the guaranty or obligation was given."

[5] Fulton *v.* Thompson, 18 Tex. 278 (1857).

[6] Hiatt *v.* Gilmer, 6 Ired. L. (N. C.) 450 (1846).

[7] Griffiths *v.* Griffiths, 2 Hare, 587 (1843).

[8] Page *v.* Wolcott, 15 Gray (81 Mass.), 536 (1860).

3. Public Licenses to Partnerships. — As each partner has authority, by virtue of the partnership relation, to do all acts required to be done in the ordinary course of the firm's business, a public license to a firm recognizes the fitness of each member to exercise the privileges of the license. Hence dissolution of a firm of retail liquor dealers, by the sale of one partner's interest to the other, ought not to work the revocation of a license issued to the firm. If the license is required as an incident of taxation, no ground for complaint on the part of the State exists. It has received its revenue from the business. If the license is required, as a police measure, to exclude unfit persons from carrying on the particular business, there is equal absence of just cause for complaint. The fitness of each partner should have been passed upon when the license was issued.[1]

4. Can a Partnership Contract with its Members? — If a firm contract is but an aggregate of the several contracts of its members, the foregoing question should receive a negative answer. Undoubtedly, a partner who has loaned money to the firm and taken its note therefor, cannot maintain an action at common law against the firm. As all of its members must be made defendants, the record would disclose that the plaintiff was suing himself. But the courts are substantially agreed that this difficulty of the common law "affects the remedy and not the right; and when the note is duly indorsed to a third person, he acquires a legal title, and may sue in his own name."[2]

The same principle applies to contracts between two

[1] Commonwealth *v.* James, 98 Ky. 30; 32 S. W. 219 (1895); Burdick's Cases on Part. 298.

[2] Woodman *v.* Boothby, 66 Me. 389 (1876); Buchanan *v.* Mech. L. & S. Inst. 84 Md. 430; 35 At. 1099 (1896); Burdick's Cases on Part. 298.

firms with a common member. At common law one firm could not sue the other on the contract. It could maintain a suit in equity, however, and the reformed procedure in some of our States permits an action to be brought by one firm against another having a common member,[1] as well as an action by a partner against the firm or by the firm against a partner.[2]

5. A Firm as a Partner. — While our law does not recognize a firm as a legal entity, it does permit it to enter into contracts as a quasi person. If a partnership and an individual execute a joint and several promissory note, the the partnership will be treated as one of the two makers, and may be sued as such by the holder; but the note will not be construed as the joint and several contract of the partners.[3]

A firm may enter a partnership as one member thereof.[4] Ordinarily a creditor's rights against such a partnership will be the same as against a firm made up of individuals.[5] If he brings an action against it, all of the persons composing it will be made defendants, and the judgment may be enforced against the property of either. In some cases, however, it is a matter of importance to the creditor, that the partnership has a firm as one of its members. The

[1] Cole *v.* Reynolds, 18 N. Y. 443 (1858).

[2] *Infra,* Chap. VI. § 4.

[3] Van Tine *v.* Crane, 1 Wend. (N. Y.) 524 (1828). In Ex parte Harding, 12 Ch. D. 557 (1879), a contract of guaranty ("we hereby guarantee," &c.) signed "Smith, Fleming & Co.," the firm name, and "John Fleming, R. McInraith, W. Nicoll," the individual names, was construed as a joint promise of the firm and a several promise of each partner.

[4] In re Hamilton, 1 Fed. 800 (1880); In re Gilbert, 94 Wis. 108; 68 N. W. 863 (1896). Creditors of the larger firm were allowed to prove against the smaller firm as though it were an individual member.

[5] Meyer *v.* Krohn, 114 Ill. 574; 2 N. E. 495 (1885).

obligation which he holds may be binding on a firm, as one member of a partnership, when it would not be binding on the persons composing that firm, if they were individual members of the partnership.

For example, Geo. C. Kidder and R. W. Kidder, composing the firm of Kidder & Bro., became a member of the partnership of Mason, Kidder & Co. For money borrowed by the larger firm, a note was given in the firm name, with the members of the firm as sureties. The name of Kidder & Bro. was signed by Geo. C. Kidder without the knowledge or consent of R. W. Kidder. It was insisted that this signature was not binding on the firm of Kidder & Bro.; but the court held that borrowing money for the larger firm, and giving negotiable paper therefor, was within the scope of the partnership business of the smaller firm, and that it was liable on this paper.[1] Had the Kidders entered the firm of Mason, Kidder & Co. as individuals, however, neither would have had authority to sign the other's name as a surety for the firm. While a partner is an agent of the firm for the purposes of its business, he is not an agent of his associates as individuals.[2]

6. Effect of a Partner's Disabilities. — As a rule, the contract rights of a firm are not affected by claims or defences against its individual members. In some jurisdictions, however, statutes have been construed as subjecting a firm to disabilities which, in terms, are imposed upon an individual. A New York statute, for example, prohibits a corporation, which has refused payment of any of its debts, from transferring any of its property to an officer or stockholder "directly or indirectly for the payment of any debt." This has been construed to prohibit the payment

[1] McLaughlin v. Mulloy, 47 Pac. (Utah) 1031 (1897); Burdick's Cases on Part. 301.

[2] Shaw v. The State, 56 Ind. 188 (1877); Terrell v. Hurst, 76 Ala. 588 (1884).

of a debt to a firm, of which a stockholder was a member. Said the court: "There is no such potency in the entity known as a copartnership as to shield a stockholder of a corporation from the penalty denounced by this statute because he happens to be a member of a firm, and thus allow him to secure to himself a preference of his claim against a corporation. If his copartner, who is not a stockholder, is injured by the enforcement of the statute, it may be a matter for adjustment between themselves, but offers no reason for suspending the operation of the statute. If the contrary doctrine were to prevail, it would result in the officers and stockholders of corporations securing to themselves indefinite preferences by forming partnership relations in which the interest in the firm profits of the partner not a stockholder would be only nominal." [1]

**§ 8. Injuries to a Firm.**

The quasi personality of a firm is brought out very clearly in actions instituted for the redress of injuries which have been inflicted upon it. In case a partnership is defamed, a joint action by its members will lie for the damages sustained by the firm.[2] If the defamation extends to the personal character of the members, as where they are charged with swindling, or perjury, they may sue as individuals, but the damages recoverable in such actions cannot include those which are sustained by the firm, and, therefore, a recovery of damages by the firm will not bar a separate action by a partner for the same defamation.[3]

1. Collusion between Partner and Outside Wrongdoer. — The fact that the injury to the firm results from collusion between a partner and an outsider does not

[1] Jones *v.* Blun, 145 N. Y. 333; 39 N. E. 954 (1895).

[2] Forster *v.* Lawson, 3 Bing. 452 (1826); Burdick's Cases on Part. 303.

[3] Duffy *v.* Gray, 52 Mo. 528 (1873).

enable the other partners to sue at law for the damages which they have suffered. Such damages could not be judicially ascertained without an accounting between the partners and a settlement of the firm's affairs. So long as the plaintiffs and the defrauding partner are associated in partnership they cannot "show any individual title or ownership in them to the partnership property or business" which they allege to have been injured by their wrong-doing associate and his fellow conspirator.[1]

If, however, a partner is damaged individually by the collusive misconduct of a copartner and an outsider he may maintain an individual action for redress. For example, should partner A fraudulently issue the negotiable paper of the firm for his individual benefit, and should the paper pass into the hands of a *bona fide* holder and be collected by him from partner B, the latter could maintain an action at law against partner A and the payee for the fraud practised upon him.[2]

[1] Sindelare *v.* Walker, 137 Ill. 43 (1891); Burdick's Cases on Part. 304.

[2] Fuller *v.* Percival, 126 Mass. 381 (1879); *cf.* Sweet *v.* Morrison, 103 N. Y. 235; 8 N. E. 396 (1886), and see *infra*, Chap. VI. § 4, 2 (*e*).

# CHAPTER IV.

## POWERS OF PARTNERS.

FREQUENT reference has been made to the implied powers of a partner. The present chapter will be devoted to a discussion of their nature and their limitations. They are implied from the partnership relation. It is not necessary for the partnership articles to enumerate them or to refer to their existence.[1] By the custom of merchants, which has received judicial sanction, each partner is "the general and accredited agent of the partnership."[2]

1. PECULIARITIES OF A PARTNER'S AGENCY. — An eminent English judge has called attention to the peculiar character of a partner's agency, in the following paragraph, which has been quoted with approval by many of our courts: "Everybody knows that partnership is a sort of agency, but a very peculiar one. You cannot grasp the notion of agency, properly speaking, unless you grasp the notion of the existence of the firm as a separate entity from the existence of the partners; a notion which was well grasped by the old Roman lawyers, and which was partly understood in the courts of equity before it was part of the whole law of the land, as it is now. But when you get that idea clearly, you will see at once what sort of

[1] "The acting partners are identified with the company, and have power to conduct its general business in the usual way. This power is conferred by entering into the partnership, and is perhaps never to be found in the articles." Marshall, C. J., in Winship *v.* Bank of U. S. 5 Pet. 529 (1831).

[2] Story on Agency (9th ed.), § 124; Bank of Australasia *v.* Breillat, 6 Moo. P. C. 152; 12 Jurist, 189 (1847).

agency it is. It is the one person acting on behalf of the firm. He does not act as agent, in the ordinary sense of the word, for the others so as to bind the others; he acts on behalf of the firm of which they are members; and as he binds the firm and acts on the part of the firm, he is properly treated as the agent of the firm. If you cannot grasp the notion of a separate entity for the firm, then you are reduced to this, that inasmuch as he acts partly for himself and partly for the others, to the extent that he acts for the others he must be an agent, and in that way you get him to be an agent for the other partners, but only in that way, because you insist upon ignoring the existence of the firm as a separate entity."[1]

(*a*) *The Entity Notion not Grasped by Parliament.* — The idea of the firm as a separate entity was not adopted by Parliament in codifying the law of partnership. The statute declares: "Every partner is an agent of the firm and his other partners, for the purpose of the business of the partnership; and the acts of every partner who does any act for carrying on in the usual way business of the kind carried on by the firm of which he is a member, bind the firm and his partners, unless the partner so acting has in fact no authority to act for the firm in the particular matter, and the person with whom he is dealing either knows that he has no authority, or does not know or believe him to be a partner."[2]

2. Classification of a Partner's Powers. — In his draft of the British Partnership Act, Sir Frederick Pollock inserted a proposed classification of the implied powers of a partner;[3] but the classification, with its distinction

[1] Jessel, M. R., in Pooley *v.* Driver, 5 Ch. D. 458 (1876).

[2] Partnership Act, 1890, § 5.

[3] Sec. 17 of his draft was as follows: "Subject to the limitations expressed in the three next following articles, every partner may bind the firm by any of the following acts: —

between trading and non-trading partnerships, was omitted by Parliament, and there is no authoritative enumeration in England of the implied powers of a partner.

(*a*) *American Statutes.* — This is true in most of our jurisdictions as well. A few States, however, have statutory provisions on the subject. The following are from the civil code of California: —

"Every general partner is agent for the partnership in the transaction of its business, and has authority to do whatever is necessary to carry on such business in the ordinary manner, and for this purpose may bind his copartners by an agreement in writing."

"A partner, as such, has not authority to do any of the following acts, unless his partners have wholly abandoned the business to him, or are incapable of acting: (1) To make an assignment of the partnership property or any portion thereof to a creditor, or to a third person in trust for the benefit of a creditor or of all creditors. (2) To dispose of the good-will of the business. (3) To dispose of the whole of the partnership property at once, unless it consist entirely of merchandise. (4) To do any act which would make it impossible to carry on the ordinary business of the partnership. (5) To confess a judgment. (6) To

"*a*. He may sell any goods or personal chattels of the firm. *b*. He may purchase on account of the firm any goods of a kind necessary for or usually employed in the business carried on by it. *c*. He may receive payment of debts due to the firm, and give receipts or releases for them. *d*. He may engage servants for the partnership business.

"If the partnership is in trade, every partner may also bind the firm by any of the following acts: *e*. He may accept, make, and issue bills and other negotiable instruments in the name of the firm. *f*. He may borrow money on the credit of the firm. *g*. He may for that purpose pledge any goods or personal chattels belonging to the firm. *h*. He may [probably] for the like purpose make an equitable mortgage by deposit of deeds, or otherwise of real estate or chattels real belonging to the firm."

submit a partnership claim to arbitration. (7) To do any other act not within the scope of the preceding section." [1]

In Louisiana, whose jurisprudence is based on the civil law, the implied powers of a partner are somewhat different from those which have been recognized by the common law. They are mainly defined in the following paragraph: —

"When there is no agreement respecting administration in the act of partnership, the following rules are adhered to. (1) The partners are supposed to have given, reciprocally, to each other the power of administering one for the other; what one does is valid, even for the share of his partners, without receiving their approbation, saving the right which they or every one of the partners has to oppose the operation before it be concluded. (2) Every partner may make use of the things belonging to the partnership, provided he employs the same to the uses for which they are intended, and he does not use them in such a manner as to prevent his partners from using them according to their rights, or against the interest of the partnership. (3) Every partner has a right to bind his partners to contribute with him to the expenses which are necessary for the preservation of the things of the partnership. (4) A partner can neither dispose of nor make any change in any real property belonging to the partnership, without the consent of his partners, should even this disposition or change be advantageous to the partnership. (5) In other than commercial partnerships a partner cannot, as partner only, and if he has not the administration, alienate or engage the things which belong to the partnership." [2]

[1] Civil Code of California, §§ 2429, 2430. This code has been re-enacted with a few modifications in Montana and North Dakota.

[2] Revised Civil Code of Louisiana, Art. 2870.

### § 1. Power to Sell Firm Property.

The nature of this implied power and some of its limitations were discussed at considerable length in the preceding chapter.[1] According to the authorities there cited, it varies with the character of the partnership business; it is never an unqualified or absolute power. The statutes, quoted above, embody this view. Indeed, the American codes go farther than the common law in limiting a partner's implied authority to dispose of firm property.

1. The Fundamental Limitation. — An excellent illustration of the doctrine, that a partner's power of sale depends upon the nature of the partnership enterprise, is afforded by a firm of farmers. A member of a mercantile firm, whose business consists in buying and selling goods, has implied authority to dispose of the entire stock;[2] but the partnership relation does not empower one of a firm of farmers to sell the animals which have been bought and are needed for use in cultivating the farm.[3] Nor, if the partnership is formed for the increase and improvement of a flock of sheep, has either partner the implied power to sell the entire flock.[4]

In such a case as the last, however, the facts imposing a limitation upon a partner's authority must be brought home to the purchaser; a topic which will be discussed in a later part of this chapter.

(a) *Incidental to the Power of Sale.* — Whenever a partner possesses authority to sell firm property, he can bind the firm by acts which are incidental to a sale. If, upon the sale of fruit trees, he stipulates that the purchaser is to pay for those only which live, the stipulation is binding upon the firm; and although the purchaser gives his

[1] Chap. III. § 3.

[2] Tapley *v.* Butterfield, Burdick's Cases on Part. 211.

[3] Cayton *v.* Hardy, 27 Mo. 536 (1858).

[4] Blaker *v.* Sands, 29 Kan. 551 (1882).

promissory note to the firm for the price of all the trees, he is entitled to be credited thereon the price of those trees which do not live.[1] Engagements by the selling partner as to the title of the property, or its fitness for a particular purpose, or its quality, which are ordinarily made upon such sales, will bind the firm as incidental to the sale transaction.[2]

(*b*) *Power of Sale may be Relinquished.* — While the *jus disponendi* of firm property is an inherent power in each member of a normal partnership, it may be relinquished by one or more of the partners, either by express agreement or by conduct.

If A, B, and C enter into partnership upon these terms: that A and B are to have the entire management of the business, while C is not to interfere, in any way, in the firm's affairs, clearly, as between themselves, C's implied agency for the firm is abandoned; and if these terms of the partnership agreement are known to the world, as in the case of joint stock companies, organized under public statutes, or are known to those dealing with the firm, C cannot bind the firm even by acts done "for the purpose of the partnership." The same result would follow, although the terms of the partnership articles were not known, provided C was a dormant partner.[3]

The authority of a normal partner to dispose of firm property may be lost by his acts. If he sells his interest in the firm, or permits it to be sold on legal process, his agency for the partnership is thereby terminated.[4] But he may mortgage his share without working such a result;[5]

[1] Hubbard *v.* Galusha, 23 Wis. 398 (1868).

[2] Sandilands *v.* Marsh, 2 B. & Ald. 673 (1819), opinion of Abbott, C. J., at 679; Sweet *v.* Bradley, 24 Barb. (N. Y.) 549 (1857).

[3] British Partnership Act, 1890, § 5, last clause; and opinion of Cleasby, B., Holme *v.* Hammond, L. R. 7 Ex. 218 (1872).

[4] See the authorities cited in Chap. VI. § 2, *infra*.

[5] Clayton *v.* Davette, 56 N. J. Eq. ; 38 At. 308 (1897); Burdick's Cases on Part. 521.

especially if the mortgagee is his copartner, and if he remains thereafter subject to all the duties and liabilities of a partner. So long as the partnership relation continues to exist between the mortgagor and mortgagee, the rights of the latter are confined to his lien on the former's share; they are not the rights of a sole owner of the stock. Even though the mortgagor agrees not to exercise the *jus disponendi* of a partner, this is but a secret restraint upon his authority, which will not affect a *bona fide* purchaser.[1]

(c) *No Implied Power to Sell for Individual Purposes.* — As a partner's agency for the firm is limited to transactions connected with its business, the validity of his sale of firm property, in payment of his individual debt, will depend upon the actual authority which his copartners have bestowed upon him, or upon the appearance of actual authority for which they are responsible.[2] The fact that the selling partner assures his creditor of his partner's actual assent to the sale, will not protect the purchaser. An agent's authority cannot be established by his declarations, as against the principal. The purchaser, in such cases, deals with the debtor partner at his peril. An unauthorized sale of this character may be ratified by the other partners, when the rights of creditors are not involved; but acts done by them, in ignorance of the facts connected with the transaction, will not establish a ratification.[3]

## § 2. Power to Incur a Firm Obligation.

Not only has a partner the implied power to divest the firm of its title to property, but the partnership relation

[1] Monroe *v.* Hamilton, 60 Ala. 226 (1877); Burdick's Cases on Part. 306.

[2] The validity of such a transfer as against firm creditors has been considered, Chap. III.

[3] Columbia Nat. Bank of Lincoln *v.* Rice, 48 Neb. 428; 67 N. W. 165 (1896); Burdick's Cases on Part. 309.

authorizes him to subject the firm to various other obligations. In the language of the California statute,[1] "Every general partner . . . has authority to do whatever is necessary to carry on such business in the ordinary manner." The acts of a partner, then, which bind the firm are those which fall within the scope of the partnership business.

1. Determining the Scope of a Firm's Business. — If the partnership articles expressly define the manner in which the business is to be conducted, they are conclusive upon the partners; and upon third persons who have notice of the terms. In the absence of such stipulations and notice, the authority of a partner "for each transaction may be implied from the nature of the business, according to the usual and ordinary course in which it is carried on by those engaged in it, in the locality which is its seat, or as reasonably necessary or fit for its successful prosecution. If it cannot be found in that, it may still be inferred from the actual, though exceptional course and conduct of the business of the partnership itself, as personally carried on, with the knowledge, actual or presumed, of the partner sought to be charged."[2]

(a) *A Question of Fact.* — In the case last cited it is said: "What the nature of that business in each case is, what is necessary and proper to its successful prosecution, what is involved in the usual and ordinary course of its management by those engaged in it, at the place and time where it is carried on, are all questions of fact, to be decided by the jury from a consideration of all the circumstances which, singly or in combination, affect its character, or determine its peculiarities; and from them all, giving to each its due weight, it is its province to ascertain and say whether the transaction in question is one which

[1] Civil Code of Cal. § 2429.

[2] Irwin *v.* Williard, 110 U. S. 499; 4 Sup. Ct. 160 (1883).

those dealing with the firm had reason to believe was authorized by all of its members."

This is undoubtedly true of a new business or of one carried on in an exceptional manner. But in old and well defined lines of business, whether a particular act is within the scope of a partner's implied authority is a question of fact to be determined by the court. In such cases, Sir Frederick Pollock has observed:[1] "There are well understood usages extending to all trading partnerships, and now constantly recognized by the court; these have become in effect rules of law."[2]

Accordingly, judges have ruled that "a copartnership formed to transport passengers and their baggage in a stage does not authorize one of the partners to bind the firm by an agreement that he will carry a person a certain distance within a specified time";[3] that a member of a firm of machinists has no implied authority to bind the firm by a promise of payment to the fund of an association, organized to keep a harbor free from ice;[4] that a law partnership does not authorize one member to bind the firm by a promise to collect a note free of charge.[5]

In the last cited case, the learned judge remarked: "We have yet to see the rare spectacle of an attorney at law, or a firm of them, rendering professional services gratuitously as a recognized and customary incident of the business in which they engage. We have long ago de-

[1] Pollock's Digest of Part. (5th ed.) 27.

[2] In Alsop *v.* Central Trust Co. (Ky.) 38 S. W. 510 (1897); Burdick's Cases on Part. 340, it is said: "In a commercial partnership the extent of a partner's power to bind the firm is a question of law, while in the non-commercial firm the power to bind his copartner is a question of fact."

[3] Walcott *v.* Canfield, 3 Conn. 194 (1819).

[4] Wells *v.* Turner, 16 Md. 133 (1860).

[5] Davis *v.* Dodson, 95 Ga. 718; 22 S. E. 645 (1895); Burdick's Cases on Part. 338.

parted from the *honorarium* from which our ancient ancestors in this noble profession either wholly or partially derived their means of subsistence."

(*b*) *Urgent but Unusual Acts.* — A partner's implied authority to incur a firm obligation being limited by the scope of its business, as above defined, it follows that his acts are not binding on the partnership, simply because they are beneficial to it,[1] or because they appear necessary in an extraordinary exigency.[2] "A power to do what is usual," it is said in the last cited case, quoting from Lindley on Partnership,[3] "does not include a power to do what is unusual, however urgent."

2. Power to Buy on Credit. — No attempt will be made to enumerate the various acts which a partner is impliedly authorized to do on behalf of his firm. Our attention will be confined to his most important and characteristic powers.

One of these is the power to purchase property on the credit of the firm. The existence of this power, in the case of an ordinary commercial partnership, has never been questioned. These associations could not properly serve the purposes for which they are organized, unless their members possessed the authority to pledge the credit of the firm for the price of "goods of a kind necessary for or usually employed in the business carried on by" them. Provided the purchase is of this character, and the seller acts in good faith, the firm will be bound, although the partner purchasing and receiving the goods misappropriates them to his own use.[4]

[1] Thomas *v.* Harding, 8 Me. 417 (1832), holding that a member of a paper manufacturing firm has no implied authority to buy, on firm credit, cloth which he can exchange for paper-rags, at a profit.

[2] Hawtayne *v.* Bourne, 7 M. & W. 595 (1841); In re Cunningham Co. Limited, Simpson's Claim, 36 Ch. D. 532 (1887).

[3] Lind. on Part. (6th ed.) 135.

[4] Bond *v.* Gibson, 1 Camp. 185 (1808); Burdick's Cases on Part. 311.

Even though the firm is not engaged in trade, its members may possess the implied power of buying certain kinds of property on firm credit.

3. Power to Hire Servants. — This power belongs to the members of non-trading as well as of trading partnerships, provided that contracts for service are incidental to the business of the particular firm. In hiring servants and appointing agents for the firm, a partner does not act in the capacity of an agent merely, and the principle that an agent cannot delegate his authority to a sub-agent has no application to him. All the partners "are regarded as being present and sanctioning the engagements and contracts which they may singly enter into within the scope of their partnership matters."[1]

4. Power to Collect Debts. — Every member of a normal partnership has implied authority to receive payment of its debts and to give receipts or releases for them.[2] He may take negotiable paper instead of cash,[3] but whether he can bind the firm, by the receipt of other forms of property, depends upon the further question, whether such act is within the apparent scope of his authority, having regard to the nature of the firm's business and the usages of those engaged in that trade or occupation.[4]

Receipts given by a partner are not conclusive evidence of payment; and even his releases may be impeached by the firm for fraud.[5]

But a partner's implied authority in the collection of debts extends beyond the mere receipt of payment. He has the power to coerce the debtor by resort to ordinary and regular legal proceedings. He may perfect a

[1] Burgan *v.* Lyell, 2 Mich. 102 (1851); Burdick's Cases on Part. 312.

[2] Major *v.* Hawks, 12 Ill. 298 (1850).

[3] Heartt *v.* Walsh, 75 Ill. 200 (1874).

[4] Lee *v.* Hamilton, 12 Tex. 413, 418 (1854).

[5] Beatson *v.* Harris, 60 N. H. 83 (1880).

mechanic's lien for the firm,[1] may employ attorneys and bring actions against firm debtors,[2] and may even execute a power of attorney under seal in the firm name.[3] In the last cited case it was said, that this exception to the common law rule, that a partner could not bind his copartner by an instrument under seal, "grows out of the necessity of the case. It is often inconvenient to bring together all the members of a firm to execute a deed of this character. The general rule is relaxed to facilitate business; and if such were not the law, great injury might result to a firm in prosecuting their claims against a party in failing circumstances, when it is important to proceed without delay."

(*a*) *Extraordinary or Improper Proceedings.* — While a partner has implied authority to institute regular legal proceedings for the firm, his power to bind his associates by a submission of their claims to arbitration is generally denied. In some jurisdictions this limitation upon a partner's power in collecting debts has been based upon his inability to bind the firm by an instrument under seal. Accordingly, where a seal was not required for a valid submission, a partner's authority to execute it for his firm was upheld.[4] The prevailing view, however, is that expressed by Baron Parke as follows: "The authority to bind a partner to submit to arbitration does not flow from the relation of partnership; and when it is relied upon, it must, like every authority, be proved either by express evidence or by such circumstances as lead to the presumption of such an authority having been conferred."[5]

In the proper and orderly conduct of regular legal pro-

[1] German Bank *v.* Schloth, 59 Ia. 316 (1882).

[2] Wheatley *v.* Tutt, 4 Kan. 240 (1867).

[3] In re Barrett, 2 Hughes, 444 (1869).

[4] Gay *v.* Waltman, 89 Pa. St. 453 (1879).

[5] Adams *v.* Bankart, 1 Cr. M. & R. 681, 686 (1835); Martin *v.* Thrusher, 40 Vt. 460 (1868).

ceedings, the act of one partner is the act of the firm. If A and B as partners recover a judgment against C, which is void because of the judge's consanguinity with A, and an officer, under A's direction, enforces the judgment against C's property, both A and B. will be liable in tort.[1] But the malicious arrest[2] or assault[3] of a firm debtor by one partner, or his groundless and malicious prosecution of a person whom he charges with larceny of firm property,[4] has been held by some courts not to be within his implied powers, and therefore not to bind the firm, unless actually authorized or ratified. The soundness of this view will be discussed at length hereafter.

(*b*) *Compromising Firm Claims.* — That the power to collect debts includes an authority to compromise them, in any honest manner, is asserted by eminent writers,[5] and has some support in judicial decisions.[6] In other jurisdictions, the authority to compromise a claim is held to depend upon the circumstances of each particular case, including the business usages of that class of partnerships in that locality.[7]

5. Power to Borrow Money. — It is customary for commercial partnerships to borrow money in carrying on their business. Hence the implied power of each partner, in a normal partnership, to pledge its credit, for money borrowed by him for the purpose of its business, has long

[1] Chambers *v.* Clearwater, 1 Keyes (N. Y.), 310; 1 Abb. App. Dec. 341 (1864).

[2] Rosenkrans *v.* Barker, 115 Ill. 331; 3 N. E. 93 (1885).

[3] Titcomb *v.* James, 57 Ill. App. 296 (1894).

[4] Marks *v.* Hastings, 101 Ala. 165; 13 South. 297 (1892).

[5] Parsons (T.) on Part. (5th ed.), § 117; Bates on Part. § 382.

[6] Cunningham *v.* Littlefield, 1 Ed. Ch. (N. Y.) 104 (1831); Doremus *v.* McCormick, 7 Gill (Md.), 49 (1848); Walker *v.* Yellow Poplar Lumber Co. 35 S. W. (Ky.) 272 (1896).

[7] Niemann *v.* Niemann, 43 Ch. D. 198 (1889); *cf.* Lindley on Part. (6th ed.) 148.

been recognized by the courts.[1] If, however, the firm conducts its business on a cash basis, this implied authority is negatived; and persons, lending money to it through one of its members, cannot hold the firm therefor, if they have notice of its business methods.[2]

Nor is this authority possessed by every member of a joint stock company, whose affairs are necessarily managed by a few of its members,[3] "for the ordinary authority of a partner is founded on the mutual confidence involved, in ordinary cases, in the contract of partnership; and this confidence is excluded when the members of the association are personally unknown to one another."[4]

The members of non-trading partnerships have no implied power to borrow money on the firm's credit. Incurring obligations of this kind is not incidental to their business. On the other hand it is unusual and as a rule unnecessary. There is, therefore, no ground for the inference that the members of such partnerships contemplated the exercise of this power, when they entered into the partnership relation. Its exercise must be actually authorized or ratified.[5]

(*a*) *Use and Abuse of this Power.*—Even when a partner possesses the borrowing power, his valid exercise of it is limited by the nature and scope of the firm's business.

[1] Rothwell *v.* Humphreys, 1 Esp. 406 (1795); Burdick's Cases on Part. 313. (Money borrowed for travelling expenses of a partner, while buying for the firm.)

[2] Hawtayne *v.* Bourne, 7 M. & W. 595 (1841).

[3] Greenwood's Case, 3 De G. M. & G. 459, 477 (1854).

[4] Pollock's Dig. of Part. (5th ed.) 30.

[5] Crossthwait *v.* Ross, 1 Humph. (Tenn.) 23, 30; 34 Am. Dec. 613 (1839). In this case it is said of a firm of physicians that if money must be raised for the needs of the firm, "it must be raised by the individuals composing the firm, and not by one member thereof, unless he be authorized by the others so to do, independent of any right arising from partnership."

He can bind the firm to repay money borrowed for carrying on the business in the ordinary manner, but he cannot pledge its credit for funds, which the lender knows he is raising in order to increase the capital of the firm, without special authority.[1] Where usury laws are in force, he has no implied authority to agree to pay more than the legal rate of interest on borrowed money;[2] nor, it is submitted, does his implied authority extend to contracts for the payment of a share of profits in lieu of interest.[3]

On the other hand, his borrowing power is not limited to cash loans.[4] The firm will be bound by his engagement in its name, although he borrows for it negotiable paper[5] or securities[6] or goods.[7]

6. Power to Issue Bills and Notes. — Another implied power possessed by the members of trading partnerships, which a partner in a non-trading firm does not possess, is that of issuing negotiable paper in the firm name.[8] Such paper is binding upon the firm, in favor of a *bona fide* holder, even though it was not issued for the purposes of the business. Inasmuch as each partner is held out by a trading firm as its general agent,

[1] Fisher *v.* Taylor, 2 Hare, 218 (1842).

[2] Dillon *v.* McRae, 40 Ga. 107, 114 (1869).

[3] Chandler *v.* Sherman, 16 Fla. 99 (1877); but see Ford *v.* McBryde, 45 Tex. 498 (1876).

[4] Blackburn Building Soc. *v.* Cunliffe, 22 Ch. D. 61 (1882); 9 App. Cas. 857 (1884). Overdrawing a bank account is obtaining a loan of money.

[5] Dietz *v.* Regnier, 27 Kan. 94 (1882); Beuttner *v.* Steinbrecher, 91 Ia. 588; 60 N. W. 177 (1895); Burdick's Cases on Part. 326.

[6] Roney *v.* Buckland, 4 Nev. 45 (1868).

[7] Adee *v.* Demorest, 54 Barb. (N. Y.) 433 (1867).

[8] In Pinkney *v.* Hall, 1 Salk. 126, Ld. Ray. 126 (1696), it is said: "By the custom of England, when there are two joint traders, and one accepts a bill drawn on both for him and partner, it binds both, if it concerns the trade; otherwise, if it concerns the acceptor only in a distinct interest and respect."

with authority to issue firm paper, it is estopped to deny as against a *bona fide* holder, that he acted as its agent in issuing a particular bill or note. "It would be a strange and novel doctrine," said Lord Ellenborough, referring to the indorsement of a trading firm, "to hold it necessary for a person receiving a bill of exchange indorsed by one of several partners to apply to each of the other partners to know whether he assented to such indorsement; or otherwise that it should be void." [1]

If the claimant, however, does not possess the rights accorded by the law of negotiable paper to a *bona fide* holder, he cannot recover against the firm, unless he can show that the paper was issued for the purposes of the business; or that the act of the partner was authorized or has been ratified by his associates.[2] In the case last cited, Lord Kenyon observed: "It is hard enough for one partner in any case to be able to bind another without his knowledge or consent; but it would be carrying the liability of partners for each other's acts to a most unjust extent, if we suffered a new partner to be bound in this manner (by the acceptance of a bill payable to the order of plaintiffs) for an old debt incurred by other persons. . . . It is no answer to say that one partner has a general power of binding the rest."

(*a*) *Burden of Proving Authority.* — This is always on the person seeking to enforce the payment of negotiable paper by a firm.[3] *Prima facie* evidence of authority in the partner, issuing the paper, to do this act, is afforded by the fact that the firm is a trading or commercial partnership; and if in addition to this, the claimant shows that he is a *bona fide* holder, the evidence of authority

[1] Swan *v.* Steele, 7 East, 210; 3 Smith, 199 (1806).

[2] Arden *v.* Sharpe, 2 Esp. 523 (1797); Sheriff *v.* Wilkes, 1 East, 48 (1800).

[3] Pease *v.* Cole, 53 Conn. 53 (1885); Burdick's Cases on Part, 314.

becomes, as we have seen, conclusive.[1] While, if the *bona fides* of his holding is negatived, and it is shown that the paper was not issued for the purpose of the firm's business, he must give proof of actual authority,[2] or of ratification.[3]

If the partnership is a non-trading one, the claimant does not make out a case against the firm, by showing that the paper in question was executed by one partner in the firm name for money borrowed for the firm.[4] In such a case he "must give evidence of the authority of the other partners to draw, accept or indorse in the firm name."[5] The fact that the paper is given for a debt which the firm admittedly owes, does not amount to the required proof. Evidence of actual authority must be given, or it must be shown that "the giving of such instruments is necessary to the carrying on of the firm business, or is usual in similar partnerships."[6]

Moreover the claimant's ignorance of the nature of the partnership will not relieve him from the necessity of giving such evidence. "When the public have the usual

[1] *Supra*, 174; Buettner *v.* Steinbrecher, 91 Ia. 588; 60 N. W. 177 (1895); Burdick's Cases on Part. 326. In this case one partner gave to the plaintiff a firm note for securities borrowed, as he assured plaintiff, for firm needs, but a part of the proceeds of which he misapplied.

[2] Leverson *v.* Lane, 13 C. B. N. S. 278 (1862). "It is plain here that, at the time the plaintiffs took the bill in question, they were perfectly aware that it was given in satisfaction of an overdue acceptance of Sterne's (the partner issuing the paper), for a matter in which the firm had no interest whatever. The case, therefore, falls within the rule that one who takes a negotiable security under such circumstances is bound to show affirmatively that the person from whom he took it had the authority of his copartners to pledge the credit of the firm."

[3] Warder *v.* Newdigate, 11 B. Mon. (Ky.) 174; 52 Am. Dec. 567 (1850).

[4] Pease *v.* Cole, Burdick's Cases on Part. 314.

[5] Levy *v.* Pyne, 1 Car. & M. 453 (1842).

[6] Smith *v.* Sloan, 37 Wis. 285 (1875).

means of knowledge given them, and no means have been suffered by the partnership to mislead them, every man is presumed to know the extent of the partnership with whose members he deals."[1]

(*b*) *Distinction between Trading and Non-Trading Firms.* — In some jurisdictions this distinction is ignored. The Supreme Court of Pennsylvania[2] has said: "No such distinction is suggested or recognized in any adjudicated cases or text-books, and there is no foundation for it in the necessities or usages of these partnerships. The necessity for borrowing money to carry on the business of a manufacturing partnership may be as great as it is in order to carry on the business of one that is strictly commercial." Undoubtedly, a firm engaged in manufacturing ought to be classed as a trading partnership.

Perhaps the difference of judicial opinion on this point is due to the fact that "there is no authoritative list or definition of the kinds of business which are 'trades' in the sense"[3] in which that term is used in classifying partnerships.

(*c*) *The Distinction is Generally Recognized.* — And yet the English courts, as well as the courts in most American jurisdictions, have recognized and enforced a distinction between trading and non-trading partnerships, when dealing with the implied power of a partner to issue negotiable paper.

Lord Denman stated the English view in the following passage: "Partners in trade have authority, as regards third persons, to bind the firm by bills of exchange, for it is the usual course of mercantile transactions so to do; and this authority is by the custom and law of merchants,

[1] Livingston *v.* Roosevelt, 4 Johns. (N. Y.) 278 (1809); see also Cooke *v.* Bank, 3 Ala. 175, 180 (1841).

[2] Hoskinson *v.* Eliot, 62 Pa. St. 393 (1869).

[3] Pollock's Digest of Part. (5th ed.) 28.

which is part of the general law of the land. But the same reason does not apply to other partnerships. There is no custom or usage that attorneys should be parties to negotiable instruments, nor is it necessary for the purposes of their business. . . . Upon the whole, we think that the implied authority is confined to partners in trade."[1]

The same view has been expressed in a carefully considered decision of the Supreme Court of Connecticut: "In a commercial partnership each acting partner is its general agent, with implied authority to act for the firm in all matters within the scope of its business; and the presumption of law is that all commercial paper which bears the signature of the firm, executed by one of the partners, is the paper of the partnership, for the reason that the giving of such notes would be within the usual course of mercantile transactions. But when we pass to non-trading partnerships the doctrine of general agency does not apply, and there is no presumption of authority to support the act of one partner."[2]

(*d*) *Definition of a Trading Firm.* — Various attempts have been made by judges and writers to define a trading firm. Chief Justice Marshall described it as one existing "for commercial purposes; for trading with the world; for buying and selling from and to a great number of individuals."[3] Mr. Justice Clifford said: "Whenever the business, according to the usual mode of conducting it, imports, in its nature, the necessity of buying and selling, the firm is then properly regarded as a trading partnership."[4] The Supreme Court of Kansas has declared that "the test of the character of a partnership is buying and selling. If it buys and sells it is commercial or trading;

[1] Hedley *v.* Brainbridge, 3 Q. B. 316 (1842).

[2] Pease *v.* Cole, 53 Conn. 53 (1885); Burdick's Cases on Part. 314.

[3] Winship *v.* Bank, 5 Pet. (U. S.) 529, 561 (1831).

[4] Kimbro *v.* Bullitt, 22 How. (U. S.) 256, 268 (1859).

if it does not buy or sell, it is one of employment or occupation." [1]

Another definition, suggested by Mr. Bates,[2] has met with approval in some jurisdictions.[3] It is this: "If the partnership contemplates the periodical or continuous or frequent purchasing not as incidental to an occupation, but for the purpose of selling again the thing purchased, either in its original or manufactured state, it is a trading partnership; otherwise it is not."

Undoubtedly every trade partnership habitually indulges in buying and selling. This habit alone, however, does not appear to furnish the basis for the legal presumption that each member of such a partnership has authority to bind it by negotiable paper. If it were the custom of merchants to buy and sell for cash only, authority to issue negotiable paper could not be presumed from the buying and selling feature of their business. And yet, as we have seen, "this authority is by the custom and law of merchants, which is part of the general law of the land." That custom was described by an early writer on partnership law as follows: "According to the present course of mercantile dealings, no sooner is a debt contracted than a negotiable security is given for it. If money is lent, if goods are sold, the lender or vendor receives a bill of exchange or promissory note from the borrower or purchaser for the payment of the sum due on a certain day." [4]

It would seem, therefore, that every partnership, whether engaged in ordinary merchandising, or in manufacturing or mechanical pursuits, is a trade partnership, in the sense now under consideration, if the regular conduct of its

[1] Lee v. Nat. Bank, 45 Kan. 8 (1890).

[2] 1 Bates on Part. § 327.

[3] Phillip v. Stanzell, 28 S. W. 900 (Tex. Civ. App.) (1895); Burdick's Cases on Part. 323.

[4] Watson on Part. (2d ed.) 195.

affairs so notoriously involves buying or selling on credit, as to warrant a court in taking judicial cognizance of its business usage in this respect.

(e) *Kinds of Business Judicially Declared to be Trades.* — The character of a partnership, engaged in carrying on the dry goods business, in the ordinary manner,[1] or in conducting a country store,[2] where articles of almost every kind are bought and sold on credit; or in the cattle trade, if the evidence shows that such a trade includes the buying and selling of cattle and the borrowing of money therefor,[3] admits of no doubt. It is a partnership organized for merchandising, and the law presumes that each partner intended to clothe the others with all the powers incident to and usually exercised by trading partners.

Even though the partners have neither a place of business, nor a continuous stock of goods, nor a common fund as firm capital, yet if they engage in a business which includes buying and selling on credit they are partners in trade.[4] The same is true of mechanics and manufacturers. While their pursuits are not commercial in the strict sense of that term, if they enter into partnership to carry on a business, involving in its ordinary conduct the buying and selling of goods on credit, their association is a trading partnership, and each partner has implied authority to borrow money on the credit of the firm, and to issue negotiable paper in its name.[5] In the case last cited it is

1 Walsh *v.* Lennon, 98 Ill. 27; 37 Am. R. 75 (1881).

2 Dow *v.* Moore, 47 N. H. 419 (1867).

3 Smith *v.* Collins, 115 Mass. 388 (1874).

4 Howze *v.* Patterson, 53 Ala. 205; 25 Am. R. 607 (1875).

5 Kimbro *v.* Bullitt, 22 How. (U. S.) 256 (1859). A partnership for running a steam saw-mill for manufacturing purposes. Said Clifford, J., "Common observation will warrant the remark that those who engage in that business always want capital to carry it on, and frequently find it necessary to ask for credit." Lanier *v.* McCabe, 2 Fla. 32 (1848), is sometimes cited as *contra,* but that decision appears to be

said: "While it is conceded that this is the law as applicable to commercial partnerships, it is insisted that it does not apply to partnerships formed for mechanical or manufacturing purposes. But no such distinction is suggested or recognized in any of the adjudicated cases or text-books, and there is no foundation for it in the necessities or the usages of partnerships. The necessity for borrowing money to carry on the business of a manufacturing partnership may be as great as it is in order to carry on the business of one that is strictly commercial: and common observation and experience show that it is equally the custom and usage of manufacturing as of commercial partnerships to borrow money to enable them to conduct their business."

(*f*) *Kinds of Business which are not Trades.* — While there is no doubt that valid partnerships may exist between lawyers and between physicians, as well as between merchants, and while the members of such firms have implied authority to do all acts which are necessary for the ordinary conduct of their business,[1] they have never been treated as partners in trade, with the implied powers of borrowing money and issuing negotiable paper. "Money," it has been said,[2] "does not constitute the business capital of an attorney and counsellor as such; nor is it the instrument with which he carries on his profession. It forms no significant item in the contributions of individuals forming a professional partnership of this character. . . . There is in the legitimate operations of such a part-

based on the ground that the partnership was a joint stock company. See *supra*, Chap. I. § 4. *Cf.* Hoskinson *v.* Eliot, 62 Pa. St. 393 (1869).

[1] Crosthwait *v.* Ross, 1 Humph. (Tenn.) 23 (1839). Partnership of physicians.

[2] Breckinridge *v.* Shrieve, 4 Dan. (Ky.) 375 (1836), cited and followed in Worster *v.* Forbush, 171 Mass. ; 50 N. E. 936 (1898). "There is no general custom or usage known to us for lawyers in partnership to give or indorse notes in the name of the partnership."

nership, no joint use of money. . . . In short, the borrowing of money is no part of the professional business of an attorney and counsellor, or of a firm associated for the pursuit of that business. It is not to be considered as coming within the scope of their ordinary transactions, unless made so by the terms of the association, or shown to be so by the practice or usage of the parties."

In some of the cases a disposition is shown to limit the implied powers of borrowing money and issuing negotiable paper to "partners in the trade of merchandise." Accordingly, a partnership in the business of tavern keeping has been judicially declared a non-trading firm,[1] and the same declaration has been made concerning a firm of printers,[2] a firm engaged in the manufacture and marketing of pottery,[3] and a firm of plumbers.[4] But the prevailing view appears to be that whether a partnership is engaged in trade or not, depends upon these questions: Is it engaged in buying and selling on credit? Does it need a joint capital? Is the issuing of negotiable paper ordinarily resorted to by firms engaged in the same line of business? If these questions with respect to a particular firm are answered in the negative, it is a non-trading partnership.

Accordingly, firms of brokers,[5] of ordinary farmers and planters,[6] of architects, ship-carpenters, and stevedores,[7] of livery stable-keepers,[8] of theatre managers,[9] of the

[1] Cocke *v.* The Branch Bank of Mobile, 3 Ala. 175 (1841).

[2] Pooley *v.* Whitmore, 10 Heisk. (Tenn.) 629 (1873); Bays *v.* Conner, 105 Ind. 415 (1885). See *contra* Porter *v.* White, 39 Md. 613 (1873).

[3] Bradley *v.* Linn, 19 Ill. App. 322 (1885).

[4] Huey *v.* Fish, 40 S. W. 29 (Tex. Civ. App.) (1897).

[5] First Nat. Bank *v.* Snyder, 10 Mo. App. 211 (1881).

[6] Kimbro *v.* Bullitt, 22 How. (U. S.) 256 (1859); McCrary *v.* Slaughter, 58 Ala. 230 (1877).

[7] Benedict *v.* Thompson, 33 La. Ann. 196 (1881).

[8] Levi *v.* Latham, 15 Neb. 509; 48 Am. R. 361 (1884).

[9] Pease *v.* Cole, 53 Conn. 53; Burdick's Cases on Part. 314.

owners and operators of thrashing machines,[1] and of real estate agents,[2] have been declared by the courts to be non-trading partnerships.

(*g*) *How Doubtful Cases are Dealt with.* — Cases are constantly brought for adjudication, which involve the powers of partners in lines of business where there are no well established mercantile customs on this subject, or where they are not so notorious as to warrant a court in taking judicial notice of them. In such cases, the power of a partner to bind the firm for borrowed money, or upon negotiable paper, is a question of fact. If the partnership is engaged in "the business of boring wells, buying materials for pumps and windmills, putting these materials together, and placing these articles into wells bored by the firm, or already bored or dug by other persons," and there is no well established usage in that line of business as to buying or selling on credit, it is error for the trial court to "hold, as a matter of law, that it is a trading partnership, and hence that each partner has implied authority to borrow money for its use, and to execute and deliver a firm note for the same." The question of authority should be left to the jury, with the instruction that the test to be applied by them is whether the borrowing of money and the issuing of negotiable paper is essential to carry into effect the ordinary purpose for which the partnership was formed; and that, in applying this test, the fact that the firm had the benefit of the money for which the paper was given, may be taken into consideration, although this fact alone does not warrant a finding that the paper is binding upon the firm.[3]

When a firm is sued on a written obligation, as, for ex-

[1] Horn *v.* Newton City Bank, 32 Kan. 518 (1884).

[2] Deardorf *v.* Thacher, 78 Mo. 128; 47 Am. R. 95 (1883).

[3] Vetsch *v.* Neiss, 66 Minn. 459; 69 N. W. 315 (1896); Burdick's Cases on Part. 328.

ample, a lease, if the plaintiff does not allege that the partnership is a trading one, the court will assume that it is a non-trading firm; and unless his complaint contains affirmative allegations "that the obligation was executed for something necessary for the transaction of the business of the firm," or that the partner issuing it was actually authorized to make the contract, or that his act has been ratified, his pleading is demurrable.[1]

7. Abnormal Partnerships in Trade. — The fact that the members of joint stock companies do not possess the implied authority which attach to ordinary trading partners, has been stated on a previous page.[2] The reason assigned for this want of authority applies to mining partnerships. Undoubtedly these firms are engaged in trade, and, in the main, they are governed by the rules of ordinary partnership law.[3] In some respects, however, they are abnormal partnerships, "with different rights and liabilities attaching to their members from those attaching to members of ordinary trading partnerships."[4]

The *delectus personæ* has no place in these associations. The necessities of their business require that their members should be numerous and that they should not be dissolved by the death or bankruptcy of a partner, or by the assignment of his interest in the firm. As new members may thus be introduced into the firm, who are personally unknown or even objectionable to the old members, there is no warrant for the inference that persons forming such

[1] Alsop *v.* Central Trust Co. (Ky.) 38 S. W. 510 (1897); Burdick's Cases on Part. 340.

[2] *Supra*, Chap. I. § 4.

[3] Patrick *v.* Weston, 22 Col. 45; 43 Pac. 446 (1895); Burdick's Cases on Part. 529. Of course, if partners in mining agree that their partnership shall be carried on as an ordinary commercial firm, it will be subject to all the legal rules applicable to such a firm. Decker *v.* Howell, 42 Cal. 636 (1872).

[4] Kahn *v.* Smelting Co. 102 U. S. 641 (1880).

associations intend that each member shall exercise the power of an ordinary managing partner.[1] He has no implied authority to issue the negotiable paper of the firm,[2] nor "to employ counsel to litigate the title of the mine."[3] His implied authority is limited to acts which appear to be necessary or usual on the part of a member in the conduct of the business.[4]

8. Implied Authority may be Negatived by the Form of the Obligation. — Even in the case of a normal trading partnership, the firm paper may show on its face that one partner had no implied power to issue it.

If the firm signature is followed by the word "surety,"[5] or it is apparent from the paper itself that it is an accommodation signature, as in the case of an anomalous indorsement,[6] or of a joint note signed by the firm and a third person,[7] every person to whom the paper is offered, has constructive notice that the signature was not given in the ordinary course of the firm's business. No one can be a *bona fide* holder of such paper. A person seeking to enforce it against the firm must prove actual authority or ratification.

If the paper is indorsed in the firm name, and is offered by the maker who is not a partner, presumptively the indorsement is for the maker's accommodation, and without other evidence than that the plaintiff paid full value to the maker for it in good faith, he cannot recover against the firm.[8]

1 Skillman *v.* Lachman, 23 Cal. 198 (1863).

2 Congdon *v.* Olds, 18 Mont. 487; 46 Pac. 261 (1896); Burdick's Cases on Part. 331.

3 Charles *v.* Eshleman, 5 Col. 107 (1879).

4 Higgins *v.* Armstrong, 9 Col. 38; 10 Pac. 232 (1885).

5 Rollins *v.* Stevens, 31 Me. 454 (1850).

6 N. Y. Fire Ins. Co. *v.* Bennett, 5 Conn. 574 (1825).

7 Rolston *v.* Click, 1 Stew. (Ala.) 526 (1828).

8 In re Irving, 17 Nat. B. Reg. 22 (1877); Burdick's Cases on Part. 334.

(*a*) *When Implied Authority is not Negatived by the Form of the Instrument.* — No such presumption exists, however, where the maker of the instrument, indorsed in the firm name, is a partner. There is nothing on the face of such paper to prevent one who pays full value for it to the maker from occupying the position of a *bona fide* holder. Whether he is entitled to this position or not, depends upon the extraneous facts attending the transfer.[1]

The same is true in the case of paper indorsed successively by two firms and transferred by a member of the firm first indorsing it. The inference from the paper itself is quite as natural that the partner transferring the paper had become the individual owner of it, as that he was disposing of it for the benefit of the first indorsing firm.[2]

9. Firm Estopped to Deny Authority. — Ordinarily a person taking firm paper from a partner in payment of his individual debt, cannot maintain an action upon it against the firm, without proving that the other partners actually authorized or ratified the act. The facts of the transaction are ample notice that the debtor partner is exceeding his implied authority.[3]

But the conduct of the firm may be such as to warrant the creditor of a partner in believing that he is authorized by his copartners to use firm paper in paying his individual debts. For example, if a firm is carrying on two banking institutions in different towns, and the partner who is cashier of bank A is accustomed to pay his individual debts

[1] Wait *v.* Thayer, 118 Mass. 473 (1875).

[2] Freeman's Bank *v.* Savery, 127 Mass. 75 (1879). In Mecutchen *v.* Kennedy, 27 N. J. L. 230 (1858), and Williams *v.* Walbridge, 3 Wend. (N. Y.) 415 (1829), which contain expressions to the contrary, there was evidence that the plaintiff did not pretend to deal with the transferring partner as indorsee, but as a partner with authority from his firm to pass the paper for his debt.

[3] *Supra*, 165; Phillips *v.* Stanzell (Tex. Civ. App.), 28 S. W. 900 (1895); Burdick's Cases on Part. 323.

to a creditor by drafts drawn as cashier to his own order, on bank B, whose manager is the other partner in the firm, and these drafts are regularly paid and retained as vouchers by bank B, with the knowledge of its manager that they were issued for his copartner's private debts, the creditor will be justified in believing that this course of dealing has the sanction of both partners. If, acting upon this belief, he sells goods or loans money to the cashier of bank A, and receives therefor the accustomed firm paper, the manager of bank B will be estopped to deny A's authority to bind the firm by this paper.[1]

10. Admissions and Representations. — Each partner has implied authority to bind the firm by admissions or representations made "concerning the partnership affairs and in the ordinary course of the business."[2] Without such authority he could not properly discharge his duties as agent of the firm. Accordingly, a statement by a partner, of the amount due from the firm to a servant, is to be treated as a statement of the firm.[3]

A partner's admissions or representations, however, which are not made in the ordinary course of the business, although they may relate to partnership affairs, are not evidence against his copartners, unless they have actually authorized or ratified them. They are receivable only against the partner making them. Hence the statement of A that he and B are partners is not evidence as against B that such a partnership exists;[4] nor is A's statement that his partner B had improperly treated a patient, admissible as against B;[5] nor is A's statement, concerning

[1] Noyes *v.* Crandall, 6 S. D. 460; 61 N. W. 806 (1895); Burdick's Cases on Part. 335.

[2] British Partnership Act, 1890, § 15.

[3] Burgan *v.* Lyell, 2 Mich. 102 (1851); Burdick's Cases on Part. 312.

[4] Hahn *v.* St. Clair Savings Co. 50 Ill 456 (1869).

[5] Boor *v.* Lowrey, 103 Ind. 468 (1885).

the business of a firm before he became a partner in it, admissible against the members of the original firm.[1]

"In order to make a declaration by one party binding on another," observed Wightman, J., in the case last cited, "it is necessary to show that the person was authorized, either generally in carrying on the business, or with reference to the particular transaction. In the present instance, however, I do not find any evidence of such authority from Tunley to Simpson, with regard to this particular transaction, or any evidence by which such an implication should necessarily arise from the situation of clerk or partner."

(*a*) *Effect of a Partner's Admissions and Representations.* — Even when the statements of a partner are admissible against the firm, they are not necessarily conclusive. Indeed, the partner who makes them may generally show that they were the result of a mistake.[2] On the other hand, they may be conclusive not only as against the member making them, but as against the entire firm. They have this effect in favor of persons who have been induced by them to alter their condition; to act otherwise than but for their reliance upon the truth of these statements they would have acted. In such cases the firm is estopped to deny their truth.

If a partner, acting within the scope of his authority, receives plaintiff's money, with directions to buy certain property and resell it; renders a statement to plaintiff that the property had been bought and resold at a profit; pays to plaintiff the proceeds of this alleged sale; represents that the firm has an opportunity to make further purchases for plaintiff and receives more money therefor, the firm is estopped to deny that any resales and profits were actually made; and plaintiff is entitled to retain the money

[1] Tunley *v.* Evans, 2 Dow. & L. 747 (1845).

[2] Hollis *v.* Burton [1892], 3 Ch. 226.

received on account of these alleged sales, as well as to recover the money last advanced.[1]

Again, in case a partner in a firm which receives plaintiff's money for investment represents that it has been invested on a particular mortgage, and pays sums to the plaintiff from time to time as interest thereon, the firm is concluded by these statements. The plaintiff's rights in equity against the firm are the same as they would have been, had the firm made the investment, and then, on the day of plaintiff's discovery of the untruth of the statements made to him, had converted it to their own use. "As one partner may certainly bind another as to any matter within the limits of their joint business, so he may by an act which, though not constituting a contract by itself, is in equity considered as having all the consequences of one."[2]

### § 2. (A.) The Power of a Partner to Execute a Firm Deed.

Common law courts, both in this country and in England, have held, uniformly, that a partner has no implied authority to bind his firm by a deed. According to these decisions, entering into contracts under seal was not an ordinary mercantile transaction, like issuing negotiable paper,[3] but such contracts were "subject to the rules of law independent of trade and commerce."[4]

Although the conclusion in these cases was based on the mistaken assumption, that contracts under seal were

[1] Rapp *v.* Latham, 2 B. & Ald. 795 (1819); Burdick's Cases on Part. 341.

[2] Blair *v.* Bromley, 1 Phillips, 354 (1847); *cf.* Coleman *v.* Pearce, 21 Minn. 123 (1879), and Griswold *v.* Haven, 25 N. Y. 595 (1862), where the firm was held liable as for a conversion of property which one partner represented it had received, but which it had not received.

[3] Harrison *v.* Jackson, 7 D. & E. 207 (1797); Burdick's Cases on Part. 343.

[4] Gerard *v.* Basse, 1 Dallas (Pa.), 119 (1784).

not mercantile instruments, the error was not fully disclosed until their doctrine had become too firmly established to be overthrown by direct assault.[1] Even the British Parliament, when codifying the law of partnership, did not disturb the doctrine.[2] It has been modified, however, by the judicial recognition of various exceptions.

(*a*) *Various Exceptions.* — Even before the decision in Harrison *v.* Jackson, the Court of King's Bench had declared that if one partner execute a deed for himself and his partner "*in the presence of that other*," it is the deed of both, although but one seal is used, and that seal is impressed upon the wax but once.[3] The "inconvenience" of the doctrine that one partner cannot bind the firm by a contract under seal, induced courts of bankruptcy, both in England and in this country, to sanction the usage which had grown up in their practice, of executing a sealed power of attorney for voting in the choice of assignees,[4] or a bond to the court upon filing a petition in bankruptcy,[5] by one partner in the name of the firm; and to treat such deeds as the deeds of the firm.

(*b*) *Seal Treated as Surplusage.* — The same "inconvenience" has led judges, in numerous cases, to treat as surplusage a seal which is unnecessary to the validity of

[1] See Macleod's Theory and Practice of Banking (4th ed., London, 1886), 236–244. The author produces an overwhelming array of evidence against this and kindred assumptions of Lord Kenyon. His comments on Mansfield and Kenyon, as expounders of commercial law, are very instructive.

[2] Partnership Act of 1890, § 6.

[3] Ball *v.* Dunsterville, 4 D. & E. 313 (1791). This decision appears to show that the explanation of the doctrine of Harrison *v.* Jackson, offered in Clark on Part. Vol. I. p. 201, as "one of the consequences of the non-recognition of the quasi person of the company firm," is incorrect.

[4] Ex parte Mitchell, 14 Ves. 597 (1808); In re Barrett, 2 Hughes (U. S. Dis. Ct.), 444 (1869).

[5] Ex parte Hodgkinson, 19 Ves. 291 (1815).

the transaction in question. For example, a chattel mortgage under seal of firm property, executed by one partner in the name of the firm, has been held as effectual against the firm as it would have been had no seal been used;[1] and a firm note under seal, issued by one partner, has been enforced against the firm, as it would have been enforced without a seal.[2]

In the case last cited, Judge Thurman expressed the opinion "that the rule, that one partner has no power to bind his copartners by deed, if not purely arbitrary, rests upon very unsatisfactory reasons"; and declared "it would be a stigma upon the law, to relieve a partnership from all liability, because the seal is affixed to an agreement, which, without it, would effectually bind the firm; or to say that although the agreement, if unsealed, would raise a presumption that it was given on partnership account, and for a consideration received or to be received by the company, yet no such presumption arises, if a scrawl is added to the partnership name."

Several States have freed themselves from the "inconvenience" of the doctrine, now under discussion, by abolishing all distinctions between sealed and unsealed instruments.[3]

(c) *Parol Authority or Ratification.* — Moreover, while common law courts have not professed to doubt the validity of the doctrine that a partner has no implied authority to execute a firm contract under seal, in this country, with a few exceptions,[4] they have repudiated Lord Kenyon's view that the executing partner's authority must be specially

[1] Tapley *v.* Butterfield, 1 Met. (Mass.) 515 (1840); Burdick's Cases on Part. 211.

[2] Purviance *v.* Sutherland, 2 Ohio St. 478 (1853).

[3] Pearson *v.* Post, 2 Dak. 220 (1880); Stimson's Am. Statute Law, § 1564.

[4] Turbeville *v.* Ryan, 1 Humph. (Tenn.) 113; 34 Am. Dec. 622 (1839).

conferred by an instrument under seal; and have held "that an absent partner may be bound by a deed executed on behalf of the firm by his copartner, provided there be either a previous authority or a subsequent parol adoption of the act."[1]

(*d*) *Sealed Instruments in the Course of Trade.* — Occasionally a court has taken even a broader view than this, and has declared that a partner has implied authority to bind his firm by a contract under seal, whenever the contract is a mercantile one and in the course of trade.[2] "I bottom my decision," said Charlton, J., in the case last referred to, "upon the broad ground that a charter party is exclusively a mercantile transaction, and always in the course of trade. . . . A charter party is as essential in the course of trade, as the negotiation of bills of exchange; and I can perceive no difference between the exigencies which would impose a liability in the one case, and destroy it in the other. This contract could not have been in the contemplation of judges when they decided that one partner could not bind the other by deed."

(*e*) *Releases under Seal.* — Under the doctrine which we have been considering, a covenant by one partner, although in the firm name, not to sue a firm debtor, will not bar a suit thereafter brought by the firm for the debt. The covenant is binding upon the partner only who executed it, and as to him it cannot operate as a release. "A covenant not to sue has been held equivalent to a release on no other principle than that of avoiding a circuity of action. . . . But if the parties opposed in interest are not the same, the principle cannot apply. If one of two plaintiffs covenants not to sue for a joint debt, he may be liable for a breach of that covenant if both afterwards

[1] Smith *v.* Kerr, 3 N. Y. 144 (1849).

[2] Straffin *v.* Newell, T. U. P. Charlton (Ga.), 163 (1808); Burdick's Cases on Part. 344.

sue. But, if he is then sued by the debtor for breach of covenant, he alone must answer for it."[1]

A *bona fide* release under seal of a firm debtor, however, does bar an action for the debt. In such a case the specialty does not operate as a grant from the firm,[2] nor as an attempt to charge the partnership with a liability. It is not upheld on the ground that one partner has power to bind his copartners by an instrument under seal. Its nature and effect are described by Chief Justice Kent, in a leading case,[3] as follows: "It is a general principle of law, that when two have a joint personal interest, the release of one bars the other;[4] and I cannot perceive that the case of copartners in trade forms an exception to the general rule. Each partner is competent to sell the effects, or to compound or discharge the partnership demands. He is to be considered as an authorized agent of the firm for all such purposes.[5] Each has an entire control over the personal estate. So, in like manner, one co-executor or administrator cannot bind his companion to an obligation, but he may commit a separate devastavit and release a debt."

(*f*) *A Fraudulent Release is not Binding on the Firm.* — While a *bona fide* release of a firm debt by one partner cannot be set aside by his copartners,[6] they are entitled to relief, when they can show that the release was fraudulent.[7] Thus, in the earlier of the two cases just cited, one of the partners, after an action had been brought by the firm against the defendant, gave to the latter a release

[1] Walmesley *v.* Cooper, 11 A. & E. 216 (1839).
[2] Hawkshaw *v.* Parkins, 2 Swanston, 539, 544 (1819).
[3] Piersons *v.* Hooker, 3 Johns. (N. Y.) 68 (1808).
[4] Ruddock's Case, 6 Coke, 25 (1592).
[5] Watson on Part. 137, 141.
[6] Furnival *v.* Weston, 7 Moore, 356 (1822).
[7] Beatson *v.* Harris, 60 N. H. 83 (1880).

from all liability to the firm. The other partner, in ignorance of this fact, brought the action to trial, and was met with the release. Thereupon he moved to set it aside, but the court held that, as one of two plaintiffs may release the action, it could not interfere "unless fraud could be imputed by direct evidence to the defendant, as well as" to the releasing partner. Such an act by the releasing partner, it was said in an earlier English case,[1] "might be improper, still it is not fraudulent," although it relieved the defendant from costs and from reimbursing the other partner for his taxable expenses in the action.

In the New Hampshire case,[2] the release was also given to the defendant by one partner, after the commencement of an action by the firm; but as the evidence disclosed that the executing partner had no interest in the firm assets and was insolvent; that the defendant had notice of these facts; that he "did not try to settle with the solvent partner, because he knew that he could not without paying the claim," and that he obtained the release without any legal consideration, the court held that the release was fraudulent and void. It would have been equally fraudulent and voidable, had it been given by the executing partner in satisfaction of a debt owing by him individually to the defendant.[3]

### § 2. (B.) A Partner's Power to Render the Firm Liable in Tort.

Thus far, in this section, we have dealt with the power of a partner to subject the firm to contractual liabilities. We have seen that his implied authority, in this respect, is determined, as a rule, by the apparent scope of the partnership business. Passing now to the consideration

[1] Arton *v.* Booth, 4 Moore, 192 (1820).

[2] Beatson *v.* Harris, 60 N. H. 83 (1880).

[3] Gram *v.* Cadwell, 5 Cow. (N. Y.) 489 (1826).

of a partner's power to subject the firm and his copartners to liabilities in tort, we shall find the same general rule obtaining. It is stated in the British Partnership Act,[1] as follows: "Where, by any wrongful act or omission of any partner acting in the ordinary course of the business of the firm, or with the authority of his copartners, loss or injury is caused to any person not being a partner in the firm, or any penalty is incurred, the firm is liable therefor to the same extent as the partner so acting or omitting to act."

1. Actual Innocence no Defence. — Although the tort be committed by one partner only, and the others are ignorant of the wrong,[2] nay, though they may have used every reasonable effort to prevent the wrong,[3] they are nevertheless answerable for the tort, provided it was done in the ordinary course of the firm's business.[4]

This doctrine, it has been observed, is "derived from the wider rule to the same effect, which is one of the most familiar and important parts of the law of agency."[5]

[1] Partnership Act of 1890, § 10.

[2] The Attorney General v. Stranyforth, Bunb. 97 (1721); Burdick's Cases on Part. 346.

[3] Limpus v. London General Omnibus Company, 1 H. & C. 526 (1862). In this case the defendants had informed their servants that they must not obstruct other omnibuses, and a servant did obstruct and overturn plaintiff's omnibus, and defendants were held liable for the damages, on the ground that the servant's act was in the course of his service. While the wrongdoer in this case was not a partner, but a servant only, the same principle of law is applicable to the wrongdoing of a partner. See next paragraph of text.

[4] Gwynn v. Duffield, 66 Ia. 708 (1885). A member of a firm of apothecaries is not acting in the ordinary course of business in giving away drugs; and for his negligence on such an occasion, his absent copartner is not liable.

[5] Pollock's Digest of Part. (6th ed.) 47. The California Civil Code declares: "The liability of general partners for each other's acts is defined by the title of Agency," § 2443.

2. A Partner is More than an Agent. — While a partner is an agent of the firm, and his acts, done within the scope of the business, bind the firm and its members precisely as these would bind them, if they were the acts of any other general agent; yet he is something more than an agent, even with respect to his copartners. This is brought out very clearly in Ashworth *v.* Stanwix.[1]

Plaintiff, a workman in the employ of Stanwix and Walker, sued the firm for injuries sustained by the negligence of Walker. Stanwix defended on the ground that Walker's negligent act was, so far as Stanwix was concerned, the act of a fellow-servant of plaintiff, and therefore plaintiff could not recover against him. The court refused to sustain the defence, although it did not question that Walker's act was of a character which would not have rendered plaintiff's employers liable, had it been done by a fellow-servant. While Walker was engaged in doing work which might have been entrusted to a mere servant, he "did not the less remain the master of the plaintiff and the partner of Stanwix."

3. Reasons Assigned for this Doctrine. — Although there is no dispute as to the existence of the rule that the firm is answerable for the torts of a member, committed in the ordinary course of the business, the reasons which have been assigned in its support are various.

Chief Justice Shaw rested it upon the principle that "when one party must suffer by the wrong and misconduct of another, it is more reasonable that he should sustain the loss who reposes the confidence in the agent, than he who has given no such confidence."[2]

[1] 3 E. & E. 701; 7 Jur. N. S. 467 (1860); Burdick's Cases on Part. 347.

[2] Locke *v.* Stearns, 1 Met. (Mass.) 560 (1840); 35 Am. Dec. 382. Action for deceit sustained against both partners, although one was ignorant that any false statements were made.

The Supreme Court of South Carolina has supported the rule upon the ground that each partner "guarantees that, within the scope of the common business, reasonable care, diligence, and skill shall be displayed by the one in charge. Or at least that a failure on the part of one thus to exercise such reasonable care, diligence, and skill is a failure in law of each and all, and an injury resulting from such failure is the act of all."[1]

In New York, an eminent judge has given as a short reason for the rule, that the partners "constitute but one person in law."[2]

4. FIRM MAY BE LIABLE FOR A PARTNER'S ILLEGAL ACT. — Some authority is to be found for the proposition, that "acts or omissions in the course of the partnership trade or business, in violation of law, will only implicate those who are guilty of them."[3] For example, it has been held that, if one member of a firm makes a usurious loan and receives from the debtor a conveyance of property as security therefor, the other partner is not liable in conversion upon the refusal of the first partner to return the property, and his retention of it for the firm, it appearing that the second partner was ignorant of the loan transaction, and that no demand had been made upon him for the

[1] Hyrne *v.* Erwin, 23 S. C. 226 (1885); 55 Am. R. 15. In an action for malpractice both partners were held liable for damages, although but one was negligent in treating the patient.

[2] Sutherland, J., in Warner *v.* Griswold, 8 Wend. (N. Y.) 665 (1832).

[3] Collyer on Part. (Wood's ed. 1878) § 473, citing Watson on Part. (ed. 1807) 235. Mr. Watson, the originator of this doctrine, neither cites any authority nor presents any argument in its support. His statement was copied, almost verbatim, by Gow and by Collyer. Having received the sanction of these writers, some American judges appear to have been content to adopt it without inquiring as to its origin, and without any examination of the judicial decisions on the subject. It is submitted that their judgments are not entitled to much weight.

property.[1] It was admitted that the New York statute, governing the transaction, declared every conveyance made to secure a usurious loan void, and that the partner negotiating the loan was guilty of conversion upon refusing to return the property in question to plaintiff upon his demand. But the court thought that, as the act of making a usurious loan was in violation of a statute and attended with a forfeiture, it could not be considered as within the scope of the business of a partnership entered into for lawful purposes. Therefore, to make the partner, who was ignorant of the transaction, liable in an action of tort, it was declared that "it must be made to appear by some other evidence, that he either authorized it or ratified it."

(*a*) *Graham* v. *Meyer criticised.* — This view, it is submitted, is erroneous. Whether a tortious act of an agent is within the scope of his employment is not determined by its legality or illegality. "In almost every action for negligent driving," remarked a distinguished English judge, when repudiating such a test, "an illegal act is imputed to a servant."[2] The partnership business in Graham *v.* Meyer[3] included the loaning of money and the receipt of securities therefor. Such an act would not be taken out of the course of the partnership business by one partner's demanding and receiving for the firm an exorbitant or even illegal rate of interest. "If one of two attorneys, who are partners, receives money collected for a client, and embezzles or absconds with it, that will form no defence to the other partner. If one should be guilty of extortion, the other would be liable to repay what had been illegally received."[4] So if one member of a firm

[1] Graham *v.* Meyer, 4 Blatch. 129 (1858); 15 Leg. Int. 25; Federal Cases, No. 5673, citing the above quotation from Collyer.

[2] Byles, J., in Limpus *v.* London General Omnibus Co., 1 H. & C. 526, 541 (1862).

[3] 4 Blatch, 129, *supra*, N. 1.

[4] Warner *v.* Griswold, 8 Wend. (N. Y.) 665 (1832).

of warehousemen refuses to surrender plaintiff's goods, unless illegal fees are paid, the entire firm must respond in damages for this wrongful act.[1] Again, a physician is liable in damages, even for a wanton act of his copartner in treating a patient of the firm.[2]

(*b*) *Breaches of Revenue Laws.* — These are attended not only by the forfeiture of the goods which illegally elude the payment of government imposts, but subject the owners of the goods to the payment of penalties. And yet to an action for the penalties, it is no defence for one partner that the breach of the revenue statute was the act of his copartner, done without his knowledge or consent.[3]

Upon this point the United States Supreme Court has said, "That, as a general rule, partners are liable to make indemnity for the tort of one of their number, committed by him in the course of the partnership business, is familiar doctrine. It rests upon the theory that the contract of partnership constitutes all its members agents for each other, and that when a loss must fall upon one of two innocent persons, he must bear it who has been the occasion of the loss or has enabled a third person to cause it. In other words, the tortious act of the agent is the act of his principals if done in the course of his agency, though not directly authorized." [4]

Counsel for the firm had argued that if a partner, in the course of his employment, wilfully does an act in violation of law, the copartner is not liable, except upon evidence that he authorized or adopted it, and Mr. Justice Field, in a dissenting opinion,[5] approved of this proposition. The majority of the court, however, repudiated it. The rea-

[1] Lockwood *v.* Bartlett, 130 N. Y. 340 (1891); 29 N. E. 257.

[2] Hyrne *v.* Erwin, 23 S. C. 226 (1885); 55 Am. R. 15.

[3] The Attorney General *v.* Stranyforth, Bunbury, 97 (1721); Burdick's Cases on Part. 346.

[4] Stockwell *v.* U. S., 13 Wall. 531, 547–8 (1871).

[5] *Ibid.* p. 562.

soning as well as the conclusions of the prevailing opinion appear to be irreconcilable with the decision of the District Court in Graham *v.* Meyer.[1]

(c) *Malicious Legal Proceedings.* — A belief in the soundness of the doctrine that acts or omissions of partners, "in violation of law, will only implicate those who are guilty of them," has led to decisions that a firm is not answerable for legal proceedings maliciously instituted by a partner, unless his acts were specially authorized or have been ratified by his copartners.[2] In such cases it is said that the malicious prosecution of offenders is not within the power constructively delegated to one partner as the agent of another.[3]

One of the earliest judicial statements favoring this view is that of Lord Eldon in Arbuckle *v.* Taylor, a case appealed to the House of Lords from the Court of Session of Scotland.[4] His remarks upon this point, however, are very meagre, and he offers no reasons in support of his conclusion, that the members of the firm, other than the one who appeared in the prosecution of Arbuckle for alleged larceny of partnership property, were not answerable for the prosecution. Moreover, this portion of his opinion is little more than a dictum, for he reached the conclusion that this action for malicious prosecution must fail, even as to the prosecuting partner, because the latter had probable cause for his prosecution.

1 4 Blatch. 129 (1858).

2 Rosenkrans *v.* Barker, 115 Ill. 331 (1885); Kirk *v.* Garrett, 84 Md. 383 (1896); 35 At. 1089.

3 Farrell *v.* Friedlander, 63 Hun (N. Y.), 254, 257 (1892); Marks *v.* Hastings, 101 Ala. 165 (1892); 13 So. 297. The language in this case is that "a prosecution for larceny of goods stolen from the firm, is not within the scope of a mercantile partnership."

4 3 Dow, 160, 186 (1815). That Lord Eldon mistook the Scotch law upon this subject is apparent from Gordon *v.* Brit. & For. Co. Session Cases, 4th Series, 75 (1886).

Upon principle, the foregoing decisions appear to be unsound.

5. ORDINARY LEGAL PROCEEDINGS. — There is no dispute that a partner is acting within the scope of the partnership business in instituting and carrying on ordinary legal proceedings, for the recovery of firm property, or for the protection of its interests, or for the redress of its wrongs.[1] It is generally agreed, also, that the partner in charge of the proceedings does not cease to be acting within the scope of the partnership business, simply by conducting them in such a manner as to inflict legal injury upon third persons. For example, if in a suit against a firm debtor, he orders an attachment to be levied on the goods of a third person, supposing them to be the goods of the debtor, his act is the act of the firm.[2] Nor will such an act be taken out of the scope of the partnership business by his knowledge that the third person has legal rights in such property with which he is unlawfully interfering.[3] Again, if one partner under a void judgment against a firm debtor takes property from the latter, and thereafter refuses to surrender it to the debtor upon demand, his acts will bind his copartner.[4] "What was done by either" partner, said the court in the last cited case, quoting the language of Judge Cooley, "in the collection of the partnership debt was presumptively with the sanction of the other."

[1] *Supra*, 69.

[2] Kuhn *v.* Weil, 73 Mo. 213 (1880).

[3] Harvey *v.* Adams, 32 Mich. 472 (1875).

[4] Rolfe *v.* Dudley, 58 Mich. 208, 211 (1885); Taylor *v.* Jones, 42 N. H. 25, *contra.* In this case it was said that "there is no legal presumption that one partner concurs in the wrongful act of another," and that it is a question for a jury whether a partner's refusal to surrender the property of a third person, which has been levied upon as the property of a firm debtor, is an act within the scope of the partnership business.

(*a*) *Orders of Arrest are Ordinary Legal Proceedings.* — If a partner is acting within the scope of the partnership business, in ordering the levy of an attachment or an execution, it is difficult to understand why he is not also acting within the scope of the partnership business, when he orders the arrest and imprisonment of a person charged with defrauding the firm, or with stealing its property. Partnerships frequently are entitled to procure the arrest and imprisonment of persons who have wronged them. Proceedings of this character, in order to be effective in protecting the rights or redressing the wrongs of a firm, must often be instituted hurriedly and be pushed vigorously. There is no opportunity for consulting all of the partners before commencing proceedings. If, in such cases, the prosecuting partner acts upon probable cause and without malice, and for the purpose of serving the interests of the firm, his acts would certainly bind all of the members. Any recovery from the arrested person would belong to the firm rather than to the acting partner.

(*b*) *Who should Suffer for a Partner's Bad Temper or Poor Judgment?* — Does the fact that this partner, through defects of temper or errors of judgment, so conducts the proceeding as to enable the arrested and imprisoned person to maintain an action for malicious prosecution, change his relationship to the firm? Does it terminate his agency? Does it put his acts outside the scope of the partnership business? If it does, what becomes of the principle "that the contract of partnership constitutes all its members agents for each other, and that when a loss must fall upon one of two innocent persons, he must bear it who has been the occasion of the loss, or has enabled a third person to cause it"? [1]

Surely it is more reasonable that the copartners who have held out this one as a fit and proper person to act in

[1] Stockwell *v.* U. S. 13 Wall. 531, 547–8 (1871).

protecting the firm's interests, should suffer for his defects of temper and errors of judgment, rather than those who have reposed no confidence in him and made no representations as to his fitness.

6. The Prosecution of Criminals. — Undoubtedly the institution of proceedings for the punishment of criminals is no part of the ordinary business of a mercantile partnership. When a partner, therefore, obtains the arrest and imprisonment of a person, not in performance of the duty which he owes to his firm to protect its interests and to obtain redress for its wrongs, but in performance of his duty as a citizen in bringing criminals to justice, he alone is answerable for his acts. As they are not done on behalf of his firm, nor to further its interests, and do not fall within the ordinary course of its business, his partners cannot be called upon to share responsibility with him.

These views are sustained by the decisions relating to the liability of employers for malicious prosecutions by their agents.[1] In a recent case, the Supreme Court of Rhode Island, sustaining a recovery of damages against a firm for plaintiff's wrongful arrest by a servant, said: "The criterion of the master's liability can never be whether the act would have been lawful for the master to have done in the circumstances as they actually existed. . . . If the servant had seen the plaintiff take up and secrete the package of spoons in question, and had allowed her to walk away with them unmolested, could any one say that he had not been derelict in his duty to his master? If, in the performance of this duty, he mistook the occasion for it, or exceeded his powers, or employed an improper degree of compulsion, the mistake and the excess must be answered for by the master. . . . The

[1] Mulligan *v.* N. Y. & Rockaway Ry. 129 N. Y. 506; 29 N. E. 952 (1892); Palmeri *v.* Man. Ry. 133 N. Y. 261; 30 N. E. 1001 (1892).

arrest was for the purpose of searching for and recovering the master's property, not with the object of punishing crime against the public."[1]

7. LIABILITY FOR A PARTNER'S FRAUDS. — For the fraudulent acts of a partner in the course of the partnership business, the firm and every member of it are liable to respond in damages. If goods are sent to a firm of commission merchants for sale, and one partner induces the owner to make a credit sale to a third person, by false representations concerning the buyer's financial condition, it is no defence to the copartners in an action for damages, that they were ignorant of the representations.[2] Again, if a firm receives goods, with instructions from their owner, "to be by them delivered to a certain person upon his paying for the same, and not otherwise," all members will be liable for conversion if any partner delivers them to the person named, without receiving payment.[3] So, if one partner forcibly and without color of legal authority seizes plaintiff's property, under the mistaken belief that his firm has a lien upon it, his copartner will be liable with him for exemplary damages.[4]

(*a*) *Actions for Deceit.* — Even in a common law action against the firm for deceit, where the plaintiff must show "that the defendants believed or had reason to believe that the representations were false at the time, and for that reason that they were fraudulently made,"[5] he makes out his case against all the partners by showing

[1] Staples *v.* Schmid, 26 At. 193; 18 R. I. 224 (1893).

[2] Castle *v.* Bullard, 23 How. (U. S.) 173 (1859).

[3] Hobbs *v.* Chicago Packing Co. 98 Ga. 576, 25 S. E. 584 (1896); Burdick's Cases on Part. 349.

[4] Robinson *v.* Goings, 63 Miss. 500 (1886); S. P. Peckham Iron Co. *v.* Harper, 41 Oh. St. 100 (1884).

[5] Oberlander *v.* Spiess, 45 N. Y. 175 (1871); Derry *v.* Peek, 14 App. Cas. 337 (1889).

that the one who made the representations believed or had reason to believe that they were false.[1]

In Chester *v.* Dickerson, cited in the last note, four partners were sued for deceit in the sale of lands. The evidence showed that two of them were engaged in perpetrating the fraud, which consisted in having petroleum poured on the lands and representing to plaintiff that this petroleum was the natural product of the lands, "but there was no evidence that Dickerson had anything whatever, personally, to do with the fraud, or that he knew that any fraud was practised." The trial court refused to charge "that they must find a verdict in favor of the defendant Dickerson, unless they believe that he personally knew or consented to some fraudulent act or representation to the plaintiffs which procured the sale," and directed the jury "that each defendant was liable for the fraud personally committed by him, and that from the time they became partners, all were liable for the fraud committed by either in and about the partnership business." The Court of Appeals, after approving the charge and the refusal to charge, declared: "It is well settled that the firm is bound for the fraud committed by one partner in the course of the transactions and business of the partnership, even when the other partners have not the slightest connection with, or knowledge of, or participation in the fraud."

8. Defamation by a Partner. — It is not necessary to show that a firm is organized for the purpose of publishing defamatory matter, in order to hold every member liable for defamation published by the firm. If the defamatory statement is made to aid the firm business, the

[1] Chester *v.* Dickerson, 54 N. Y. 1 (1873); Peckham Iron Co. *v.* Harper, 41 Oh. St. 100 (1884); Brundage *v.* Mellon, 5 N. D. 72; 63 N. W. 209 (1895); Burdick's Cases on Part. 348. *Contra*, Stewart *v.* Levy, 36 Cal. 159 (1868).

partnership will be responsible for it. Accordingly if a partner in a manufacturing firm falsely publishes that a rival manufacturer is infringing a patent which they own, that they have secured an injunction and closed up his business, each partner is answerable in damages for the defamation.[1] "Each of the partners," to quote from the decision in the last cited case, "is an agent of the partnership as an entirety, and, if in the course of that business he injures the business of another by slander, the partnership is liable therefor, just as it might be for any other tort by any other agent."

(*a*) *Malicious Intention of a Partner.* — By statute, in Massachusetts, the truth of the words published is not an absolute defence: "The plaintiff may, notwithstanding the words are true, maintain his action if he can show that they were published with malicious intention." In case the words are published in the course of a firm's business, will the fact that one partner only was responsible for the publication, absolve his absent, ignorant, and innocent partners from liability? The Supreme Court of Massachusetts has answered the question in the negative.[2] In the case referred to, defendants, as partners in the publication of a newspaper, were sued for publishing false and malicious libels of the plaintiff. At the trial they "asked the judge to rule that express malice of one of the defendants could not affect the other defendants, unless it appeared that they participated in such malice. The judge refused so to rule," and, on appeal, the Supreme Court held that the refusal was right. "Partners," it was declared, "are the general agents of each other and of the firm; and the reason for imputing the actual malice or fraud of an agent to his principal, is not that it is inferred that the

[1] Haney Manufacturing Co. *v.* Perkins, 78 Mich. 1; 43 N. W. 1073 (1889).

[2] Lothrop *v.* Adams, 133 Mass. 471 (1882).

principal actually participated in the malice or fraud, but, the act having been done for his benefit by his agent acting within the scope of his employment in his business, it is just that he should be held responsible for it in damages."

(*b*) *Defamation not in the Course of Business.* — It is not enough to bring the publication of a libel within the course of the partnership business, that it was authorized by a partner and referred to a partnership transaction. In a comparatively recent case,[1] one member of a firm of furniture dealers placed the following placards on a table: "This was taken back from Dr. Woodling, as he would not pay for it; for sale at a bargain," and "Moral: Beware of dead beats." As it appeared very clearly from the evidence that the libellous matter was published not as a firm advertisement, but for the purpose of venting the personal spite of the partner who actually published it, the court held that the action was properly dismissed as to the partner who knew nothing about the placards.

9. Punishment of the Innocent Partner. — While every member of a firm is answerable in damages for the tort of any member, committed in the course of the partnership business, he is not subject to punishment therefor, if he is actually innocent of any wrongdoing. For example, a proceeding under a statute for the arrest and punishment of debtors, who have disposed of their property to defraud creditors, cannot be maintained against all of the partners, upon evidence that a fraudulent disposition of firm property has been made by one partner. Such a statute does not include debtors who have been guilty of no personal delinquency.[2]

A similar view has been taken of statutory provisions for the arrest of defendants in actions for fraud. The

[1] Woodling *v.* Knickerbocker, 31 Minn. 268; 17 N. W. 387 (1883).

[2] Watson *v.* Hinchman, 42 Mich. 27; 3 N. W. 236 (1879).

North Carolina Code of Civil Procedure authorizes the arrest of a defendant "when the defendant has been guilty of a fraud in contracting the debt," etc. This language, it has been held, does not warrant the arrest of an innocent partner, in an action for damages by one who had been induced to sell goods to the firm by false representations of the copartner.[1]

Under a similar statute in New York, the Court of Appeals has held [2] that in an action to enforce a contract for the purchase of property made by his agent, the defendant cannot be arrested on proof that the vendor was induced by the agent's fraud to enter into the contract, when the fraud was not known to the defendant, nor authorized nor ratified by him, on the ground that the statutory "test of the liability to arrest in such an action is the guilt of the defendant in contracting the debt or incurring the obligation sued upon." Whether the defendant would have been liable to arrest, had the plaintiff brought his action for deceit, was not decided.

10. Liability for a Partner's Misapplication of Property. — We have seen that every member of a partnership is liable for the wrongful conversion of a third person's property by any partner, while acting in the course of the partnership business. But it must be borne in mind that the mere fact that the wrongdoer is a member of a firm will not make his copartners answerable for his misconduct, even though "had he not been connected with the firm he might not have been in a position to commit the" wrong.[3]

The leading case in England on this point is Ex parte Eyre,[4] in which a customer of a banking firm attempted to

[1] McNeeley *v.* Haynes, 76 N. C. 122 (1877).

[2] Hathaway *v.* Johnson, 55 N. Y. 93 (1873). See Nat. Bank of Comm. *v.* Temple, 39 How. Pr. 432 (1870).

[3] Lindley on Part. (6th ed.) 173.

[4] 1 Phillips, 227 (1842).

hold all the partners liable for the abstraction by one partner of securities from a box deposited with the firm. It appeared, however, that the customer gave to this partner authority to borrow certain securities from the box, upon his substitution of others; and that the partner, after substituting certain securities, abstracted them, without the knowledge of his copartners. It was held that "the act was a tortious act committed by one partner, not acting for the partnership or for any partnership object, but in his separate character, and for his own individual and separate purposes."

The doctrine of this case has been applied frequently in this country. For example,[1] the owner of certain shares of stock sent them to B with a power of attorney to him to sell them. Instead of selling the shares, he had them transferred to his firm, but they always remained in his custody, his copartners knowing nothing of the affair, until their failure, when the stock was discovered in his private drawer, and was handed to them by the firm's assignee. The court held that the owners of the stock had no claim against the firm; that they confided the stock to B as an individual, and that the subsequent transactions with the stock were not those of his firm, but were B's transactions alone.

(*a*) *Temporary Possession of the Property by the Firm.*—In cases of the character now under consideration, when a partner obtains property, not in the course of the partnership business, but in his individual capacity, the further fact that the firm receives and holds the property for a time, will not of itself render the copartners liable for the property.

A good illustration of this doctrine is afforded by Toof *v.* Duncan;[2] also a case where the wrongdoer's connection

[1] Adams *v.* Sturges, 55 Ill. 468 (1870).

[2] Toof *v.* Duncan, 45 Miss. 48 (1871).

with the defendant firm gained for him the opportunity of committing the wrong. Frazier, while on a trading expedition for his firm, was asked by Duncan to collect and remit to him a debt due from a party in another town to which the firm business was expected to take Frazier. The latter assented, and Duncan drew his draft on the debtor to Frazier's order. Instead of presenting it in person, Frazier indorsed it to his firm for collection, and after it was collected received the proceeds from his firm and used them for his individual purposes. Inasmuch as Duncan's transaction was with Frazier individually, and as the firm derived no benefit from the money, but paid it over to Frazier in good faith and without any knowledge of Duncan's arrangement with him, the court held that Frazier alone was responsible to Duncan, and that the other partners were not "in any way, morally or legally, involved in the transaction."[1]

(*b*) *Liability for Property Fraudulently Acquired by a Partner.* — A case quite similar to the last, but differing in some important respects, has received the careful consideration of the New York courts.[2] The Rittenhouse Manufacturing Company made a fraudulent purchase of goods from the plaintiffs; its president pledged them for a loan; deposited the lender's check, for the sum loaned, with a firm composed of Ammidown, the president and chief stockholder of the company, and A. D. Smith, and soon after, but before plaintiffs had discovered the fraud,

[1] *Cf.* Dounce *v.* Parsons, 45 N. Y. 180 (1871). Plaintiff was induced by one partner to supply him with money to be used for a specific purpose. Instead of using it for that purpose, he deposited it with the firm as his own money, and checked it out in payment of debts for which he was liable, but not for debts of his firm. His copartners, who were ignorant of plaintiff's transaction with him, were held to be under no liability to plaintiff.

[2] Bienenstock *v.* Ammidown, 155 N. Y. 471 (1898); 49 N. E. 321, reversing s. c. in 29 N. Y. Supp. 593, 32 N. Y. Supp. 1138, 11 Misc. 76.

drew out the money in payment of the company's debts. The company and Ammidown were insolvent. The trial court gave judgment against both Ammidown and Smith, on the ground, among others, that the receipt of the money by the firm was a partnership transaction with the company. This was affirmed by the general term, but reversed by the Court of Appeals.

It was admitted by the lower courts that Smith had no personal knowledge of the company's fraud, and that the firm of Ammidown and Smith received no benefit from the transaction. But in the opinion of those courts, the knowledge of Ammidown was imputable to Smith when the check was deposited by the company with the firm. Moreover, they declared that the receipt of the check by the firm was a transaction of the partnership in the ordinary course of its business; that the check, at the time Ammidown indorsed it to his firm, could have been recovered by the plaintiffs; and that the firm by taking title to the check, collecting it and paying out the proceeds upon orders of the Rittenhouse Company, became liable to the plaintiffs therefor.

(c) *Not in the Course of the Partnership Business.*— Had the check been received by the firm in the ordinary course of its business, and had its proceeds gone into the general funds of the firm, Smith would have been liable to plaintiffs, even though he had been personally ignorant of the transaction, and even though Ammidown had checked out the proceeds for the benefit of his company. The case would have been governed by the rule laid down in the famous Fauntleroy forgery cases in England,[1] and which has been followed in this country.[2]

[1] Marsh *v.* Keating, 2 Cl. & F. 250 (1834); Stone *v.* Marsh, 6 B. & C. 551 (1827). The rule is now formulated in the British Partner-

[2] Guillon *v.* Peterson, 89 Pa. St. 163 (1879). In this case one partner loaned to his firm certain securities which he held as executor;

But in Bienenstock *v.* Ammidown, it appeared that the Rittenhouse Company had an arrangement with Ammidown & Smith, permitting it to deposit moneys with the firm against which it could draw at any time; that the check in question was deposited to the company's credit, and the full amount thereof drawn out by the company within two or three days after the deposit. Although in a sense it was a partnership transaction to receive the deposit, yet that circumstance, in the opinion of the Court of Appeals, was so "qualified and materially affected by the fact that it was a mere accommodation extended to the customer, from which the firm could derive no benefit, having no interest in such deposits, and holding the same subject to immediate draft," that the firm was not charged with the "liability which might follow upon a regular and ordinary business transaction, in the conduct of which Ammidown would be acting as its agent as well as that of the company."

(*d*) *Whether a Transaction is in the Course of the Business* — is often a difficult question of fact; a question upon

ship Act of 1890, § 11, as follows: "In the following cases, namely: (*a*) Where a partner, acting within the scope of his apparent authority, receives the money or property of a third person and misapplies it; and (*b*) Where a firm in the course of its business receives money or property of a third person, and the money or property so received is misapplied by one or more of the partners while it is in the custody of the firm, the firm is liable to make good the loss."

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another partner sold them and applied the proceeds to the payment of firm debts. All the partners were held liable to the estate for the securities, although some of them were ignorant of the transaction. Said Paxson, J.: "It is entirely within the course of the regular business of the firm to pay its debts. I regard the case in hand as stronger than those cited, for the reason that the firm got the benefit of every dollar realized from the securities, while in Marsh *v.* Keating, 2 Cl. & F. 250, and Stone *v.* Marsh, 6 B. & C. 551, Fauntleroy cheated his firm, as well as the owner of the stock, by appropriating to his own use the money received from the sale of the stock."

which learned judges have frequently differed, even when the evidence was undisputed. Bienenstock *v.* Ammidown, which we have been reviewing at some length, is an example. Another illustration is afforded by Cleather *v.* Twisden,[1] in which Justice Denman held, that the receipt and misappropriation of certain bonds by a member of a firm of solicitors, were acts in the scope of the partnership business, while all of the judges of the Appellate Court were of the opposite opinion. Said Bowen, L. J., "Although we differ from Mr. Justice Denman in the conclusion at which we have arrived, that difference arises solely from the different view we take of the facts. We agree entirely with him in his view of the law. This is a case which falls very near the line."

In other cases the question is an easy one. If a partner in a mercantile firm collects money for a third person and uses it in the firm business, instead of remitting it to his principal, the partnership and every member will be liable for the amount.[2] Although his acts as collector were not in the ordinary course of the partnership business, he was exercising an implied power as a partner in borrowing and using the money. His acceptance of a draft for the money in the firm name would bind the firm, as an act done in the ordinary course of the partnership business.[3]

11. Wrongful Use of Trust Funds by a Partner. — If all the members of a firm assent to the wrongful use of trust funds, in the firm business, by one of their number, all will be liable to the *cestui que trust*, not because of their partnership relation, but because they are joint wrongdoers. But a partner who improperly uses trust

[1] 28 Ch. Div. 340 (1884). Still another example is Rhodes *v.* Moules [1895], 1 Ch. 236, reversing Kekewich, J.

[2] Welker *v.* Wallace, 31 Ga. 362 (1860); Whittaker *v.* Brown, 16 Wend. (N. Y.) 504 (1836).

[3] Palmer *v.* Scott, 68 Ala. 380 (1880).

funds in the partnership business as his own property, does not render the partnership a debtor to his *cestui que trust.*[1]

It is true that the *cestui que trust* may be able to recover his property from the firm "if he can show that the firm still has it, and that the firm did not come by it by purchase for value without notice. The true owner of money traced to the possession of another has a right to have it restored, not because it is a debt, but because it is his money. His right is incidental to his ownership; and whether the money is traced to the hands of a single individual, or to the hands of a firm, is immaterial."[2]

If he cannot show that the firm still has the funds, his claim will be confined to the wrongdoing partner.[3] The same result will follow where the trust money is paid by the trustee partner as his contribution to the firm capital.[4] The rights of the firm and of the other partners are substantially those of purchasers for value, and if they have no notice of the trustee partner's fraud, they will incur no liability to the *cestui que trust*, by receiving and using his contribution to the capital of the partnership.[5]

(*a*) *Notice of the Fraud.* — It is not necessary to prove that his copartners had actual knowledge of the trustee partner's fraud upon his *cestui que trust.* Knowledge of facts fairly putting them upon inquiry, which, if followed up, would have disclosed the truth, is enough to

[1] Ex parte Apsey, 3 Brown's Ch. Ca. 265 (1791). *Cestui que trust* not allowed to prove against firm estate. Jaques *v.* Marquand, 6 Cow. 497 (1826); Shaffer *v.* Martin, 25 App. Div. (N. Y.) 501 (1898).

[2] Lindley on Part. (6th ed.) 178; Randall *v.* Knevals, 27 App. Div. (N. Y.) 146 (1898).

[3] Englar *v.* Offutt, 70 Md. 78; 16 At. 497; 14 Am. St. R. 333 (1889).

[4] Gilruth *v.* Decell, 72 Miss. 232; 16 So. 250 (1894); Burdick's Cases on Part. 351.

[5] Hollembaek *v.* More, 44 N. Y. Super. Ct. 107 (1898).

fix upon all the partners responsibility for the wrongdoing partner's acts.

In some cases, the knowledge of the defrauding partner is imputed to his innocent copartners.[1] But this ought not to be done when the fraudulent act is outside the scope of the partnership business, or where it amounts to a fraud [2] upon his copartners as well as upon outsiders. Accordingly, if a partner obtains his wife's money, by forging her name to a check, and uses it as his contribution to the capital of his firm, his knowledge of the fraud is not imputable to his copartners, as his "acts and doings" are "wholly outside the scope of the partnership business." [3]

(*b*) *Why Defrauding Partner's Knowledge is not Imputable to his Partners.* — This topic received very careful consideration in Bienenstock *v.* Ammidown,[4] a case which was briefly stated on a preceding page. In the lower courts it was ruled that Ammidown's knowledge

[1] Randall *v.* Knevals, 27 App. Div. (N. Y.) 146 (1898); Cunningham *v.* Woodbridge, 76 Ga. 302 (1886).

[2] Bignold *v.* Waterhouse, 1 M. & S. 255 (1813).

[3] Gilruth *v.* Decell, 72 Miss. 232; 16 So. 250 (1894); Burdick's Cases on Part. 351.

[4] 155 N. Y. 47; 49 N. E. 321 (1898). The provisions of the British Partnership Act of 1890, bearing upon the questions decided in this case, are as follows: "§ 13. If a partner, being a trustee, improperly employs trust-property in the business or on the account of the partnership, no other partner is liable for the trust-property to the persons beneficially interested therein: Provided as follows: (1) This section shall not affect any liability incurred by any partner by reason of his having notice of a breach of trust; and (2) Nothing in this section shall prevent trust money from being followed and recovered from the firm if still in its possession or under its control." "§ 16. Notice to any partner who habitually acts in the partnership business of any matter relating to partnership affairs, operates as notice to the firm, except in the case of a fraud on the firm committed by or with the consent of that partner."

of the Rittenhouse Company's defective title to the check, which he deposited to its credit with his firm, was imputable to his copartner. The Court of Appeals, however, repudiated this view. "Ammidown," it declared, "in temporarily depositing the proceeds of property fraudulently acquired by him for his manufacturing company with his firm, without any communication of thè fact to his copartner, would be conducting a fraud upon him, if in so doing he could make him incur an unsuspected and unusual liability to a third person. The rule of law which attaches a responsibility to the status of a partnership relation for the acts of a copartner, within the scope of business transactions, is founded upon a just view of the requirements of public commercial interests. To extend its operation to the extent of imputing the notice or knowledge of one copartner, acquired in transactions outside of the partnership business, and which were had for his individual benefit, to the other, would be to convert the rule into an instrumentality of injustice."

## § 2. (C.) Powers of the Majority.

The articles of partnership often provide that in case of differences or disputes between the members relating to the firm business, the determination of the majority, or the decision of a particular member, shall be binding upon all. A provision of this character in the partnership agreement is not only legal, it is most desirable. In the absence of such a stipulation, however, the decision of a majority is binding upon all the partners, provided it relates to the ordinary business of the firm, and is made in good faith.[1]

[1] British Partnership Act of 1890, § 24 (8) declares: "Any difference arising as to ordinary matters connected with the partnership business may be decided by a majority of the partners, but no change may be made in the matter of the partnership business without the consent of all existing partners."

1. ORDINARY MATTERS OF PARTNERSHIP BUSINESS. — In commenting upon the subsection of the Partnership Act quoted in the last note, Sir Frederick Pollock states that "Sir G. Jessel is believed to have intimated in one or more unreported cases an opinion that a majority of the partners has not any power whatever implied by law. But the rule that in such matters the mind of the greater number must prevail is universal in modern business practice."[1]

This rule has the sanction of judicial[2] and of legislative authority[3] in this country. It is thought to be more reasonable and just to imply an understanding on the part of all the members of the firm, that the will of the majority shall prevail in all matters within the scope of the partnership business, than "to allow the minority to stop the operations of the concern, against the views of the majority."[4]

When persons associate themselves as partners, they invest the firm with the power to do all acts required to be done in the ordinary course of the business which is to be carried on by the firm. In this respect, a partnership differs from an association of tenants in common. The latter do not form a business entity, and their titles to

[1] Pollock's Digest of Part. (6th ed.) 79.

[2] Peacocks *v.* Chambers, 46 Pa. 434 (1863); Burdick's Cases on Part. 353. In this case, the owners of a majority of the shares of the partnership stock were held entitled to discharge an agent and to employ another, notwithstanding the dissent of a strong minority.

[3] See Civil Code of California, § 2428: "Unless otherwise expressly stipulated, the decision of the majority of the members of a general partnership binds it in the conduct of its business." But *cf.* La Rev. Civ. Code, Art. 2870.

[4] Johnston *v.* Dutton, 27 Ala. 245, 253 (1855). Plaintiffs recovered on notes given in the firm name by two of three partners, for goods sold to the firm by plaintiffs, after notice that the third partner refused to be responsible for further debts of the firm.

the property held in common are several titles. Their relationship to each other and to the common property affords no such ground for inferring an understanding that the minority is to abide by the decision of the majority, as exists in case of a partnership.[1]

In the case last cited, two of the three members of a firm brought an action in the firm name, upon a contract made by the firm, to collect what was alleged to be due upon it. "Such conduct," the court held, "is within the power of the majority, because it is within the scope of the business of the firm and in furtherance of it. A dissenting minority has no veto power in such a case, but is bound by the action of the majority."

The sale of partnership goods, being an ordinary matter of the firm's business, may be made by a majority of the partners, and in the absence of fraud or collusion the purchaser will acquire a perfect title, although he is notified by the minority that they do not consent to the sale.[2]

2. Limits to the Power of the Majority. — While the minority cannot veto an act which has been decided upon by the majority in good faith, and is within the ordinary scope of the partnership business, its members have the right to veto any act which is outside the ordinary affairs of the firm.

If the articles of a trading partnership provide that the business shall not include the purchase and sale of spirituous liquors, the business cannot be so changed as to include this traffic without the consent of every partner.[3]

[1] Irvine *v.* Forbes, 11 Barb. (N. Y.) 587 (1852); Clarke *v.* Slate Valley Ry. 136 Pa. 408; 20 At. 562 (1890). In the latter case, it appearing that the majority, who gave the warrant of attorney to proceed with the case, had divested themselves of all interest in the firm, an order, staying proceedings until a sufficient warrant of attorney should be filed, was sustained.

[2] Staples *v.* Sprague, 75 Me. 458 (1883).

[3] Jennings' Appeal, 16 At. (Pa.) 19 (1888).

So, if the articles declare that the business shall be carried on at a designated place, or in such other place as the partners may agree upon, nothing short of the consent of every partner to a change of location will authorize such a change. The assent of all the partners to a lease of certain premises for their business will authorize the location of the business upon those premises. Upon the expiration of the lease, however, the renewed consent of all will be necessary to authorize a renewal of the lease and the continuance of the business there.[1]

3. THE MAJORITY MUST ACT IN GOOD FAITH. — Even when the majority are engaged in a transaction, which is within the ordinary scope of the firm business, they are bound to act in good faith towards the minority. "For a majority to say, 'We do not care what one partner may say, we, being the majority, will do what we please,' is" to act in bad faith. The minority should have an opportunity to express their views; and the conclusions of the majority should represent their honest opinions of what is best for the firm as a whole. The majority should meet "not for the purpose of negativing what any one may have to offer, but for the purpose of negativing what, when they are met together, they may after due consideration think proper to negative."[2]

Accordingly, if the majority, after hearing the dissent of a member, and learning that their proposed act will operate as a fraud upon him, arbitrarily decide to do the act, their act will be invalid, so far as his interests are concerned. A bill of sale of firm property, in such circumstances, will not convey the firm title to a purchaser with knowledge of the facts.[3]

[1] Clements *v.* Norris, 8 Ch. D. 129 (1878).

[2] Lord Eldon in Const *v.* Harris, Turn. & R. 496 (1824).

[3] The Western Stage Co. *v.* Walker, 2 Ia. 504 (1856).

§ 2. (D.) **Effects of Dissent.**

Not only are the acts of the majority binding upon all of the members, when done in good faith and in the ordinary course of the partnership business, but their disapproval of a particular course of action must be heeded by the minority, as well as by third persons who have notice of it.

For example, if two of three partners refuse to give preferences and determine to turn out the firm property for *pro rata* distribution among the firm creditors, the third partner cannot give a valid mortgage on the partnership assets to a firm creditor who is aware of these facts. In such a case the implied power possessed by each partner to mortgage firm property for firm debts is revoked, and the majority are entitled to have the mortgages cancelled.[1]

1. Dissent by One of Two Partners. — If the firm is composed of but two members, the effect of dissent by one will depend upon the nature of the act involved. It is quite clear that one partner cannot annihilate the power of his copartner to receive payment of firm debts, by notifying the creditors that they must not pay to the copartner.[2] Nor, according to the weight of authority, can he, by dissent, destroy the implied power of his copartner to pay a firm debt, or to mortgage firm property to secure it, even though the consequence of the payment or security is to prefer a favored creditor.[3] If, however, the purpose and effect of a transfer of the firm assets by one partner are to

[1] Carr *v.* Hertz, 54 N. J. Eq. 127; 33 At. 194 (1895); Burdick's Cases on Part. 356.

[2] Gillilan *v.* The Sun M. I. Co. 41 N. Y. 376 (1869). In this case there was no evidence of fraud or collusion, although the partner receiving payment was insolvent.

[3] Mabbett *v.* White, 12 N. Y. 442 (1855); Burdick's Cases on Part. 212.

immediately terminate the partnership, and to place all of the property beyond its control, the dissenting partner may be able to have it set aside in equity.[1]

Again, if both partners have assented to a firm contract, which is determinable at the option of the partnership, either partner can keep the contract in force, even against the wish of his copartner.[2] On the other hand, as we have seen, if the contract is limited to a definite period, neither partner can renew the contract without the other partner's assent.[3] In such cases, as the authority of the partners is coextensive, the partner who refuses his assent to a change has the advantage of position.[4]

2. New Obligations. — The principle just stated operates to prevent one partner from imposing new obligations on the firm, against the dissent of his copartner, if this is communicated to the obligee, although they may be within the ordinary scope of the firm business. We have seen that either member of a trading firm has implied authority to issue firm paper. If, however, one partner, in a firm of two, refuses to permit the issue of firm paper, a creditor, taking such paper from the copartner, with notice of the refusal, cannot enforce it against the firm. "Nothing can be more reasonable," it has been said, "than that a person may protect himself, in this manner, against the fraud and misconduct of his associate. The principle under consideration is not founded at all on any supposed waiver by the creditor, but solely and exclusively on the declaration of the person declining to be bound. The implied

[1] McGrath *v.* Cowen, 57 Ohio St. 385 ; 49 N. E. 338 (1898).

[2] Donaldson *v.* Williams, 1 Cr. & M. 345; 3 Tyrwh. 371 (1833). One partner undertook to dismiss a weekly servant, against his copartner's will; but the dismissal was held ineffective.

[3] Clements *v.* Norris, *supra*, 218.

[4] Butchart *v.* Dresser, 4 De G. M. & G. 542 (1853); Burdick's Cases on Part. 363. One partner can make a valid transfer of firm property in carrying out a firm contract, although his copartner objects.

authority of his partner he has annihilated; and the contract in the name of the firm is of no validity, beyond the personal obligation it infers on the individual making it."[1]

(*a*) *Waiver by Dissenting Partner.* — Although one partner by dissenting may withdraw from his copartner the authority impliedly conferred by the partnership relation, his subsequent conduct may amount to a waiver of this withdrawal. In Wilkins *v.* Pearce, referred to in the last note, one partner borrowed from Pearce his acceptance of a draft and gave Pearce an agreement in the firm name to take care of the draft at maturity. The copartner refused to assent to this agreement; yet, later, he received the draft and applied it to the use of the firm. "His application of the acceptance to the partnership use," it was held,[2] "was inconsistent with his previous dissent, and ought to be regarded as a waiver of it, and a ratification of the stipulation in the partnership name to provide for the draft at maturity."

So, if the partners agree that all purchases by the firm shall be for cash, neither partner has the right to waive the stipulation. But in case goods are bought on credit by one partner and used by the firm, both partners are liable for the price. "A partner, not bound by the act of his associate in its inception, assumes the obligation when he takes the benefit of the property thus acquired, and

[1] Leavitt *v.* Peck, 3 Conn. 124 (1819). In Wilkins *v.* Pearce, 5 Den. 541 (1848), it is said: "By the act of entering into a copartnership each of its members becomes clothed with full power to make any and every contract within the scope and limits of the copartnership business. . . . This power is incident to the copartnership relation, and must exist, in defiance of expostulations and objections, while the relation endures." But in that case, there was evidence that the dissenting partner had waived his dissent. See this case, in the Court of Appeals, cited in the next note.

[2] Pearce *v.* Wilkins, 2 N. Y. 469, 472 (1849).

assents to its going into the common stock, as truly as if the right to bind the firm in the premises existed." [1]

§ 2. (E.) **Notice of Limitations on a Partner's Power.**

In the cases last cited, those dealing with the partner had received express notice of the limitations upon his authority. Such notice is not necessary, however. The form of the notice is immaterial. "Circumstances may speak as forcibly as words." [2] Notice of restrictions upon a partner's implied authority is sometimes given by the form and contents of a writing (such as a promissory note), which is a part of the transaction.[3]

In a recent case,[4] it appeared that Wilson and Cassells, partners under the name of Wilson, Cassells, & Co., had agreed that no money should be borrowed for the firm, except upon notes payable to Wilson's order and indorsed by him, and that plaintiff had discounted a number of notes in that form. Later, Cassells presented to plaintiff two notes, signed by him in the firm name to the order of Wilson, with Wilson's name indorsed thereon without authority, and one note in the firm name to plaintiff's order. Plaintiff discounted them, and Cassells used the money for his own benefit. It was contended for Wilson that the form of the notes was notice to plaintiff that the money to be obtained upon them was for Wilson individually, and that Cassells's authority, as a partner, to borrow money for the firm had been limited by agreement between him and Wilson. The trial court declined to take this view, and its ruling was affirmed on appeal. The form of the

[1] Johnston *v.* Bernheim, 86 N. C. 339 (1882); Mason *v.* Partridge, 66 N. Y. 633 (1876).

[2] Carr *v.* Hertz, 54 N. J. Eq. 127; 33 At. 194 (1895); Burdick's Cases on Part. 356, 359.

[3] *Supra*, 184.

[4] International Trust Co. *v.* Wilson, 161 Mass. 80; 36 N. E. 589; Burdick's Cases on Part. 361.

notes was a matter for the jury to take into consideration, in determining whether the plaintiff had notice of the agreement, but such notice was not to be inferred as matter of law from the form of the notes. "It is obvious," said the court, "that the same form might have been used if Cassells's authority had been unlimited."

### § 3. Powers of a Partner after Dissolution.

To say that a partnership has been dissolved is to say, that the relation which has subsisted between persons who were carrying on a business in common, with a view of profit, has been terminated. As soon as this relation is broken up, the powers of the associates, which we have found to be conferred by the relation, are withdrawn. If new business engagements are entered into, they are binding upon the individuals who have made or have actually authorized them, but upon no others. They are not binding upon the firm, for that has ceased to exist. They are not binding upon the members of the dissolved firm, who are not actual parties to them, for the actors are no longer their agents. All this, upon the supposition that the firm has not only been dissolved, but that due notice of dissolution has been given, in accordance with the rules presented in a former chapter.

1. Performing Existing Contracts. — While the dissolution of a partnership terminates the authority of each partner to enter into new engagements for the firm or for his former associates, it does not destroy his power to act for them in "matters in which they all still have a common interest, and are under a common liability." [1]

Such a common interest and common liability exist in the case of a contract made by the firm, and unperformed at dissolution. Neither partner is at liberty to say to the

[1] Gates *v.* Beecher, 60 N. Y. 518 (1875); Burdick's Cases on Part. 372, 375.

other contracting party, our firm is dissolved, the contract is therefore at end, and you must not tender performance. Even after notice of dissolution, the third party may perform the contract and call upon all the partners for satisfaction. If the contract is for the sale of goods to the firm, the seller may recover the price from the members, although he delivers them after notice of dissolution.[1] It follows, therefore, that the implied authority of each partner to receive and pay for the goods continues.

(a) *Other Examples.* — If the contract is for the services of a firm of attorneys, the client's right to the ability and skill of all the partners is not affected by the dissolution of their partnership. Services thereafter rendered by either partner are subject to the terms of the firm contract. If a particular rate or method of compensation has been agreed upon, this must be observed by the partner rendering service;[2] and for the acts of the partner, who is allowed to transact the business, his former copartners are liable. He is engaged in discharging their obligations as well as his own.[3]

Again, if the contract calls for the erection of a building by the firm, the dissolution of the partnership does not discharge the contract. And if the dissolution is caused by the death of a member, the survivor has full power to complete the building, and charge the deceased partner's interest in the firm with its proportion of the expenditures incident thereto.[4] Moreover, if a firm has executed a mortgage on its property to secure a third person for money which he has agreed to furnish for the erection of buildings thereon, the mortgage lien will include moneys

[1] Whiting *v.* Farrand, 1 Conn. 60 (1814).

[2] Moses *v.* Bagley, 55 Ga. 283 (1875).

[3] Smyth *v.* Harvie, 32 Ill. 62 (1863); Williams *v.* Whitmore, 9 Lea (Tenn.), 262 (1882).

[4] Rust *v.* Chisolm, 57 Md. 376 (1881).

advanced to the surviving partner as well as those advanced before the firm's dissolution.[1]

(*b*) *New Obligations Incidental to the Performance of Existing Contracts.* — Although the dissolution of a firm terminates the authority of its members to transact any new business, the performance of existing contracts often necessitates the creation of new obligations. In such a case, the new obligation should be treated as merely incidental to the performance of a common duty, and thus, within the implied authority of either partner. It is believed that the weight of authority supports this view.

In a leading case,[2] upon this point, it appeared that a firm of sharebrokers had entered into a contract for the purchase of certain railway shares. After dissolution, in order to raise money with which to pay the balance due for the shares, one partner pledged them with the bankers of the former firm. This, it was held, he had power to do. Said Lord Justice Turner, "Each partner has, after and notwithstanding the dissolution, full authority to receive and pay money on account of the partnership, and has the same authority to deal with the property of the partnership, for partnership purposes, as he had during the continuance of the partnership. This must necessarily be so. If it were not, at the instant of the dissolution, it would be necessary to apply to this court for a receiver in every case, although the partners did not differ on any one item of the account. Nor is there any inconvenience in this state of the law; for it is competent to any partner to apply, in case of necessity, for a receiver, and to have the affairs of the partnership wound up under the direction of this court, and thus to prevent his partner from exercising unduly any power which he has as a partner."

[1] Rust *v.* Chisolm, 57 Md. 376 (1881).

[2] Butchart *v.* Dresser, 10 Hare, 453 (1853); s. c. on appeal, 4 De G. M. & G. 542 (1853); Burdick's Cases on Part. 363.

In another case,[1] where the defence interposed was the absence of authority in one partner to issue negotiable paper in the firm name, it appeared that the paper was given pursuant to an agreement of the firm to renew certain notes when they matured; and the court held that the dissolution of the firm did not revoke the authority of either partner to renew the paper. Power to perform the firm contract necessarily included the power to create the new obligation for which the contract provided.

2. Contracts Terminated by Dissolution. — The doctrine, which we have been considering, does not apply to contracts, which, although continuing engagements in form, are to be construed as terminable by the dissolution of the firm.[2] For example, if a firm, engaged in conducting a lottery, contracts to pay its counsel a certain sum per month "during the existence or operation of said lottery," the agreement is to be construed as terminating with the existence of the firm.[3] The same construction has been put upon contracts with firm agents appointed to sell a note,[4] or "buy and sell goods, sign notes, and perform all acts concerning the business."[5] The dissolution of the firm terminates the agency.

Moreover, agreements of a firm may be binding on it only as offers, as when it undertakes to supply another with such goods as he may order, or guarantees payment for such goods as A may purchase of B. In such cases the duly notified dissolution of the firm works a revocation of the offer. If after such notice the third person orders

[1] Richardson *v.* Moies, 31 Mo. 430 (1862); Burdick's Cases on Part. 366.

[2] See *supra*, 151. For example of a contract not so terminable, see Horst *v.* Roehm, 84 Fed. 565 (1898).

[3] Lochrane *v.* Stewart, 2 S. W. (Ky.) 903 (1887).

[4] Robb *v.* Mudge, 14 Gray (80 Mass.), 534 (1860).

[5] Schlatter *v.* Winpenny, 75 Pa. 321 (1874).

the goods, or B sells to A, neither partner has any implied authority to bind his former associates by accepting the order or by promising to pay B.[1]

3. Implied Authority to Wind up the Business. — Not only do the members of a firm retain their implied powers to complete subsisting contracts after dissolution, but these powers extend to all acts necessarily involved in winding up its affairs.

Lord Eldon declared on several occasions[2] that while in one sense a partnership was determined by dissolution, in another sense it is "continued till all the affairs are settled." Similar expressions are to be found in the opinions of other distinguished judges, both in England and in this country. Chancellor Kent has said: "A dissolution of a partnership only has respect to the future. The parties remain bound for all antecedent engagements. The partnership may be said to continue as to everything that is past, and until all pre-existing matters are wound up and settled."[3] In a leading English case,[4] Mr. Justice Heath declared: "With regard to things past, the partnership continues and always must continue." This form of statement has been criticised by writers and judges. Mr. Justice Lindley has characterized it as a loose statement which increased rather than diminished the difficulties of the courts.[5]

[1] See Caldwell *v.* Stileman, 1 Rawle (Pa.), 212 (1829); Goodspeed *v.* Wiard Plow Co. 45 Mich. 322 (1881).

[2] Ex parte Williams, 11 Ves. 3; 8 R. R. 62 (1805); Crawshay *v.* Maule, 1 Swanston, 495; 1 Wil. 181; 18 R. R. 126 (1818); Wilson *v.* Greenwood, 1 Swanston, 471 (1818).

[3] Griswold *v.* Waddington, 16 Johns. 438, 493 (1819). This, like Lord Eldon's statement on the subject, was a mere *dictum*. *Cf.* Story on Part. (7th ed.) § 325.

[4] Wood *v.* Braddick, 1 Taunt. 104; 9 R. R. 711 (1808).

[5] Lindley on Part. (5th Eng. ed.) 218. The correctness of this view is shown in Raulett *v.* Collier White Lead Co. 30 La. Ann. 56 (1878), where the court found it necessary to limit the *dicta* of earlier cases.

(*a*) *The Statutory Rule in Britain.* — In accordance with Mr. Justice Lindley's suggestion, a more guarded statement of the rule upon this topic was embodied in the British Partnership Act.[1] It is as follows: "After the dissolution of a partnership the authority of each partner to bind the firm, and the other rights and obligations of the partners, continue, notwithstanding the dissolution, so far as may be necessary to wind up the affairs of the partnership, and to complete transactions begun but unfinished at the time of the dissolution, but not otherwise. Provided that a firm is in no case bound by the acts of a partner who has become bankrupt, but this proviso does not affect the liability of any person who has after the bankruptcy represented himself or knowingly suffered himself to be represented as a partner of the bankrupt."

This statement of the rule, although not as broad in terms as the *dicta* above referred to, appears to accord with the weight of actual decisions in this country as well as in England. In some of our States, the authority of partners, after dissolution, has been further restricted by statute.[2]

[1] Partnership Act of 1890, § 38.

[2] The following provisions in the California Civil Code have been re-enacted in Montana and North Dakota: "Article VI. Liquidation. § 2458. After the dissolution of a partnership, the powers and authority of the partners are such only as are prescribed by this article. § 2459. Any member of a general partnership may act in liquidation of its affairs, except as provided by the next section. § 2460. If the liquidation of a partnership is committed, by consent of all the partners, to one or more of them, the others have no right to act therein; but their acts are valid in favor of persons parting with value, in good faith, upon credit thereof. § 2461. A partner authorized to act in liquidation may collect, compromise, or release any debts due to the partnership, pay or compromise any claims against it, and dispose of partnership property. § 2462. A partner authorized to act in liquidation may indorse, in the name of the firm, promissory notes, or other obligations held by the partnership, for the purpose of collecting the same,

4. Authority to Dispose of Firm Assets. — Upon the dissolution of a partnership each partner "is entitled to have the whole assets disposed of . . . for the purpose of settling the rights between the partners."[1] In the absence of agreement that one or more of the partners shall act as liquidators, each of them "has an equal right to the possession of its assets, and is under an equal duty to apply those assets to the discharge of the debts."[2] It follows, therefore, that after dissolution, as before that event, "each partner still has authority to dispose of the partnership property, to collect, adjust, and pay debts, and give proper acquittances."[3]

(a) *The Power to Sell.* — That each partner may exercise this power, after dissolution, in the absence of agreement to the contrary, is undisputed. Some courts, however, hold that the power ceases as soon as the debts of the firm to outside creditors are paid. This doctrine is based on the theory that "after dissolution partners are tenants in common, with no right in either" to sell the interest of the others, except so far as might be necessary to settle up the partnership affairs and pay the partnership debts.[4]

but he cannot create any new obligation in its name, or revive a debt against the firm, by an acknowledgment, when an action thereon is barred under the provisions of the code of civil procedure."

[1] Wild *v.* Milne, 26 Beavan, 504 (1859); Burdick's Cases on Part. 166.

[2] Gray *v.* Green, 142 N. Y. 316, 320; 37 N. E. 124; 40 Am. St. R. 596 (1894).

[3] Van Keuren *v.* Parmelee, 2 N. Y. 523, 525–6 (1849).

[4] Brewer, J., in Hogendobler *v.* Lyon, 12 Kan. 276, 281 (1873). A similar statement in Stair *v.* Richardson, 108 Ind. 429 (1886), is referred to in Needham *v.* Wright, 140 Ind. 190 (1895); Burdick's Cases on Part. 260 n., as "an inadvertent expression . . . unnecessary to the decision of that case."

It has been shown, in an earlier chapter[1] that this conception of partnership title is erroneous. Moreover, when a receiver is appointed to wind up the affairs of a partnership, his power to sell property does not cease with the satisfaction of the claims of outside creditors. He converts the entire assets into cash, and, after paying outside creditors, distributes the remainder between the partners in accordance with their claims upon the firm.[2]

It is to be borne in mind, however, that while each partner can transfer the firm title, after dissolution, he cannot, in connection with the sale, bind his late partners by a new and distinct contract, such as a covenant in an assignment of a judgment recovered by the firm, that all the judgment debtors remained liable upon the judgment.[3]

(b) *The Power to Pledge Firm Property.* — That this power belongs to a surviving partner is well settled.[4] We have seen that the English courts[5] accord it also to each partner, after dissolution *inter vivos*, provided he employs it in winding up the firm's affairs. There is some judicial authority[6] in this country, too, for this view, which it is submitted is entirely sound. On the other hand, the continuance of a partner's power to pledge firm property after dissolution has been denied.[7]

[1] *Supra*, Chap. III. See Rice *v.* McMartin, 39 Conn. 573 (1873); Bach *v.* The State Ins. Co. 64 Ia. 595 (1884).

[2] *Infra*, Chap. VIII.

[3] Bennett *v.* Buchan, 61 N. Y. 222 (1874).

[4] Bohler *v.* Tappan, 1 Fed. 469 (1880); Breen *v.* Richardson, 6 Col. 605 (1883). In the latter case, a trust deed of firm realty by the surviving partner was held valid; its purpose and effect being to prevent a sacrifice of the property.

[5] Butchart *v.* Dresser, 4 De G. M. & G. 542 (1853); Burdick's Cases on Part. 363.

[6] Miller *v.* Florer, 15 Ohio St. 148, 153 (1864).

[7] Roots *v.* Salt Co. 27 W. Va. 483 (1886).

In the last cited case, the learned judge writing the opinion remarked, "There can, I presume, be no question as to the law, that none of the partners can, after the dissolution of the partnership, without the consent of the others, buy or sell or pledge goods or other property on account of the partnership," citing as his leading authority Story on Partnership, § 322. It is true, that Judge Story did say, in that section, that "none of them can buy or sell or pledge goods on account thereof," but this language was used with reference to the statement in the preceding clause of the same sentence, viz.: "None of the partners can create any new contracts or obligations binding upon the partnership." In §§ 325 to 328, the distinguished author explains fully his views concerning the implied powers of partners after dissolution. He carefully limits the foregoing statement to new transactions "in the course of the former trade," and announces as the admitted doctrine of the common law, that the dissolution of the firm "leaves every partner in possession of the full power (unless, indeed, upon the dissolution it has been exclusively confided and delegated to some other partner or person) to pay and collect debts due to the partnership; to apply the partnership funds and effects to the discharge of their own debts; to adjust and settle the unliquidated debts of the partnership; to receive any property belonging to the partnership; and to make due acquittances, discharges, receipts and acknowledgments of their acts in the premises."

5. Power to Give and to Indorse Firm Paper. — If each partner possessed this power after dissolution, it would be possible for him to postpone indefinitely the settlement of partnership affairs, as well as to impose upon his copartners new contracts, which are not necessary and incidental to winding up the business of the firm. It is uniformly held, therefore, that this power does not sur-

vive partnership dissolution. In order to bind the firm as a party to negotiable paper after dissolution, the partner issuing or indorsing it in the firm name must have actual authority therefor from his associates.[1]

In some jurisdictions, it is thought to follow necessarily from the doctrine just stated, that the title of a firm to paper, payable to its order, cannot be transferred even by an indorsement without recourse. It is said "that such an indorsement is a contract, and would imply certain obligations on the part of the firm, though they could not be charged as indorsers."[2]

Other courts have held that a partner, under his implied power to sell firm property, may effectually transfer paper payable to its order, by indorsing it without recourse.[3] This is certainly the better view; for the obligations of the firm growing out of such a transfer are substantially the same as those which attend the sale of paper payable to bearer,[4] or the sale of other firm property.[5]

6. Power to Pay and Settle Firm Debts.—The only differences of opinion here relate to the extent of this authority. It is admitted that a partner may pay debts, not only by turning over cash, but by transferring firm property to the creditor in satisfaction of his claim.[6] If the amount due is in dispute, a *bona fide* settlement by the creditor with one partner is binding upon all. For mere mistakes or errors in judgment, on the part of the acting

[1] Potter *v.* Tolbert, 113 Mich. 000; 71 N. W. 849 (1897); Burdick's Cases on Part. 367.

[2] Fellows *v.* Wyman, 33 N. H. 351, 356 (1856), following Sanford *v.* Mickles, 4 Johns. (N. Y.) 224 (1809).

[3] Yale *v.* Eames, 1 Met. (42 Mass.) 486 (1840); Waite *v.* Foster, 33 Me. 424 (1851).

[4] Parker *v.* Macomber, 18 Pick. (Mass.) 505 (1836).

[5] See British Bills of Exch. Act, 1882, § 58; Neg. Inst. Law of N. Y. ch. 612, Laws of 1897, § 115.

[6] Milliken *v.* Loring, 37 Me. 408 (1854).

partner, his adjustment of the claim cannot be set aside.[1] If the copartners are not willing to trust each other in adjusting doubtful liabilities, they should apply for a receiver.

7. Expenses of Winding Up. — The implied authority of each partner to convert the firm property into cash and apply it to the satisfaction of firm debts, cannot be exercised without incurring expense. Oftentimes the preservation of firm property necessitates new outlays. For expenditures of such a character, therefore, either partner may bind not only the firm property, but his former associates.[2] Contracts, however, for improving the property which are not incidental to its preservation, or to its conversion into money, he has no implied power to make.[3]

8. Admissions of Liability. — Upon this point the conflict of authority is irreconcilable; and, curiously enough, the leading cases[4] on each side were decided in the same year. In each case the question at issue was whether one partner, after dissolution, could bind his copartner by a statement of the amount of the debt owing by the firm at the time of dissolution. Each court considered the case a perfectly clear one; so clear that any extended statement of its reasons was deemed unnecessary; but the conclusions reached by the courts were diametrically opposed.

In the English case, Mansfield, C. J., said, "Since it is clear that one partner can bind the other during all the partnership, upon what principle is it that from the moment

[1] Bass *v.* Taylor, 34 Miss. 342 (1857); Moist's Administrator's Appeal, 74 Pa. St. 166 (1873).

[2] Conrad *v.* Buck, 21 W. Va. 396, 413 (1883).

[3] Stebbins *v.* Willard, 53 Vt. 665 (1881).

[4] Wood *v.* Braddick, 1 Taunt. 104 (1808); Burdick's Cases on Part. 369; Hackley *v.* Patrick, 3 Johns. (N. Y.) 536 (1808). Opinion quoted in full, Burdick's Cases on Part. 371. For the modern authorities on each side of this question, see 40 Am. St. R. 567 (1894). See also Hart *v.* Woodruff, 24 Hun (N. Y.), 510 (1881); Burdick's Cases on Part. 370.

when it is dissolved, his account of their joint contracts should cease to be evidence?" The Supreme Court of New York (consisting of Kent, Ch. J., Thompson, Spencer, Van Ness, and Yates, JJ.) said: "This is a clear case; after dissolution of copartnership the power of one partner to bind the other wholly ceases. There is no reason why his acknowledgment of an account should bind his copartner any more than his giving a promissory note in the name of the firm, or any other act. The plaintiff ought to have produced other evidence of the debt."

Probably no better statement of the rule which ought to prevail on this subject, has ever been made than the following: "After a dissolution, however caused, the new words and acts of those who were partners shall have no effect upon the rights or obligations of their former copartners, excepting so far as these words and acts fairly belong to the settlement of the concern, and the power which each partner has in winding it up."[1]

9. Taking Firm Debts out of the Statute of Limitations. — Whether the power, which a partner possesses before dissolution, to waive the benefit of the statute of limitations,[2] continues after dissolution is another question upon which the authorities are divided.

It ought to be held that this power is unaffected by a dissolution of which due notice is not given. A creditor receiving part payment or a new promise from a partner, in such circumstances, has a right "to rely on it as a partnership act, with the incidents and legal consequences of such an act."[3] And this is the prevailing view.[4]

[1] Parsons on Part. (4th ed), § 128; Barnes v. Northern T. Co., 169 Ill. 112; 48 N. E. 31 (1897).

[2] Goodwin v. Parton, 41 L. T. Rep. 91 (1879).

[3] Sage v. Ensign, 2 Allen (84 Mass.), 245 (1861); Forbes v. Garfield, 32 Hun (N. Y.), 389 (1884); Clement v. Clement, 69 Wis. 599; 35 N. W. 17 (1887).

[4] *Contra*, Tate v. Clements, 16 Fla. 339; 26 Am. R. 709 (1878).

When due notice of dissolution has been given, however, the power of either partner to subject the firm or his copartners to a new obligation ceases. The proper determination, therefore, of the question which we are now considering "depends upon another, that is, whether the acknowledgment or promise is to be deemed a mere continuation of the original promise, or a new contract, springing out of and supported by the original consideration."[1] For a considerable period, the statute of limitations was not regarded with favor by the courts, whose hostility led them to treat it as founded on the presumption of payment. During this period, it has been said, "One who was spoken to on the subject of an old debt, could not well give a civil answer, without saying enough to take the case out of the statute."[2] It is now treated by the judiciary as a beneficial statute, designed to afford security against stale demands, and to produce speedy settlements of accounts. This modern conception of the statute has resulted in the doctrine, generally accepted, that an acknowledgment or promise which will take a precedent debt out of the statute must amount to a new contract, although a contract founded upon the original consideration. Wherever this doctrine is accepted, it is held that neither part payment of the old debt nor a new promise to pay it, made by one partner, after dissolution, will bind the others, without proof of authority, in addition to the former partnership relation, to make the payment or the promise on their behalf.[3]

(*a*) *The Minority View.*— Although this doctrine prevails generally in England and in this country, it is not accepted by all of our courts. The minority view is rested

[1] Bell *v.* Morrison, 1 Pet. (U. S.) 351, 371 (1828).

[2] Van Keuren *v.* Parmelee, 2 N. Y. 523; 51 Am. Dec. 322 (1849).

[3] Watson *v.* Woodman, L. R. 20 Eq. 721, 730 (1875); Davis *v.* Poland, 92 Va. 225; 23 S. E. 292 (1895); and cases in the last two notes.

at present not upon principle but upon precedent. A brief and unreasoned judgment of Lord Mansfield is at the bottom of this judicial heresy. He declared that "payment by one" of four makers of a joint and several promissory note "is payment by all, the one acting, virtually, as the agent for the rest; and in the same manner, an admission by one is an admission by all, and the law raises the promise to pay when the debt is admitted to be due."[1] Partners are joint debtors. Therefore, it is said, each partner, even after dissolution, is "by force of the rule of law proceeding from the case of Whitcomb *v.* Whiting," "empowered as their agent to stop, as against his associates, the running of the statute."[2]

In the case last cited, Chief Justice Beasley declared: "It is enough for me to know that the rule in question has, for many years, been regarded by my predecessors as the settled law of this State; that it rests upon respectable grounds, to say the least of it, and that, in its operation upon the affairs of business, it has not been attended with any serious inconveniences. Under such conditions, I think the rule cannot be abolished, even though it should seem that it is not entirely reconcilable with the highest ideal of a perfect theory of the legal subject to which it appertains.[3]

(*b*) *Payment or New Promise after Statutory Period.* — Some of the courts, holding the minority view, limit the power of a partner to payments and new promises made by him before the expiration of the statutory period. The Supreme Court of New Jersey has expressed the opinion that "the doctrine that a joint debt, when not barred by the statute, can be revived as against all the original debtors by the unauthorized act of one of them, has neither reason

[1] Whitcomb *v.* Whiting, 2 Doug. 652 (1781).

[2] Merritt *v.* Day, 38 N. J. L. 32; 20 Am. R. 362 (1875).

[3] *Cf.* statement by Royce, J., in Mix *v.* Shattuck, 50 Vt. 421, 424; 28 Am. R. 511 (1878).

nor justice for its support."[1] In other jurisdictions, no distinction is made "whether the promise or acknowledgment was before or after the statute had run. The debt is none the less morally and justly due," say these courts, "whether a longer or a shorter time has elapsed since it was contracted."[2]

(*c*) *If Statute Pleaded, Lex Fori Prevails.* — As the statute of limitations regulates and restricts the right of suing, the *lex fori* and not the *lex loci contractus* will determine which of the foregoing doctrines is applicatory in a particular case. Therefore, although the legal effect of a partner's part payment or new promise, in the State where it is made, is to prolong the running of the statute or to remove the statutory bar, this will not avail the plaintiff who sues in a State where the law denies such effect to a partner's act.[3] "When the *lex fori* says that a suit cannot be maintained, then it cannot be maintained, notwithstanding it is in force by the *lex loci contractus*."[4]

10. Power to Dishonor Negotiable Paper. — While the members of a partnership are jointly liable on negotiable paper issued by the firm, they are not joint obligors simply. The distinction between the negotiable paper of joint makers who are not partners and that of a partnership "rests upon the fact that partners are but one person in legal contemplation. . . . And so a demand of one partner is sufficient because he represents the firm, and a dishonor by one is a dishonor by all, and each is presumed to have authority to act for the others; while in the case of a note of joint makers, not partners, the indorser has

[1] Parker *v.* Butterworth, 46 N. J. L. 244, 254 (1884); s. p. Hicks *v.* Lusk, 19 Ark. 692, 694 (1858).

[2] Wheelock *v.* Doolittle, 18 Vt. 440, 442 (1846).

[3] Mayberry *v.* Willoughby, 5 Neb. 368; 25 Am. R. 491 (1877); Kerper *v.* Wood, 48 Ohio St. 613; 29 N. E. 501 (1891).

[4] Wharton's Comm. on Am. L. § 335.

a right to rely upon the responsibility of all and each, and may insist upon a dishonor by each." The dissolution of a partnership does not change the nature of the contract it made when it issued a promissory note; nor can such subsequent event modify the indorser's contract on the paper. The indorser's engagement was to pay, if the maker, that is the partnership, did not pay on due presentment, and if due notice of dishonor was given to him. After dissolution, as before, the partners have a common interest in having firm paper paid, they have a common liability thereon, and each is legally chargeable with knowledge of the firm's ability and willingness to pay. "Again the purpose of demand and notice to the indorser is that he, being informed of the failure to pay by the partnership, may be put at once on his guard, to save himself, if may be, from loss. This end is achieved when one of former partners has refused to pay, as when all have." Such is the reasoning of the courts, leading to the conclusion that a demand of payment, made at the proper time and place, of one partner and his refusal are a dishonor of the paper, whether the partnership has been dissolved or not, and that due notice of such dishonor to the indorser fixes his liability.[1]

(*a*) *Power to Waive Presentment, Demand, and Notice.* — In the case of paper indorsed by a partnership, either member may waive presentment, demand, and notice even after dissolution, as this act does not impose a new obligation upon his associates, but is incidental to adjusting existing liabilities.[2] If the indorsing firm has been discharged from liability, however, by the holder's failure

[1] Gates *v.* Beecher, 60 N. Y. 518 (1875); Burdick's Cases on Part. 372.

[2] Seldner *v.* Mt. Jackson Bank, 66 Md. 488; 59 Am. R. 190 (1886); *cf.* Cady *v.* Shepherd, 11 Pick. 400; 22 Am. Dec. 379 (1831), holding that a partner can change place of delivery after dissolution.

to make demand and give notice, a subsequent promise by one partner to pay the paper will bind only himself. He cannot re-obligate his associates without their assent.[1]

11. Powers of a Liquidating Partner. — Although, upon dissolution, the power of winding up the affairs of the firm is committed to a single partner, by agreement, his implied authority is not thereby increased. Such an agreement is construed, save in Pennsylvania,[2] as withdrawing powers from the others but not adding to the powers of the liquidator. He "becomes the agent of the partnership for the one specific purpose. His duty is to collect and adjust debts due to the firm, to turn the assets into money, to pay and discharge the outstanding liabilities, and then to pay over to the other partners their just shares of the remaining surplus."[3]

[1] Schoneman *v.* Fegley, 7 Pa. St. 433 (1848); Myers *v.* Standart, 11 Ohio St. 29 (1860).

[2] Estate of Davis, 5 Whart. 530; 34 Am. Dec. 574 (1840).

[3] Gilmore *v.* Ham, 142 N. Y. 1; 36 N. E. 826; 40 Am. St. R. 554 (1894); Woodson *v.* Wood, 84 Va. 478; 37 A. L. J. 389 (1888).

# CHAPTER V.

## RIGHTS AND REMEDIES OF CREDITORS.

### § 1. Firm Creditors at Law.

We have seen that the members of a firm are not only jointly liable for its debts, but that they are personally liable to the extent of their several fortunes for all firm obligations.[1] In other words, the creditors of a firm are also the creditors of the several partners. We have discovered, also, that the common law does not recognize a partnership as a legal entity. Therefore, common law actions by and against a firm must proceed in the names of its members and not in its business name.[2]

1. The Property which may be Reached. — Firm creditors, who institute common law proceedings against the partners, are not limited to firm property, for the satisfaction of their claims. Nor are they bound to exhaust the assets of the firm, before levying process upon the individual property of a partner. As soon as they obtain judgment, or issue execution, its lien covers individual as well as firm property. "The judgment is several, the writ runs against the defendants as individuals."

[1] *Ante*, Chap. III. § 6 (A).

[2] Lewis *v.* Cline, 5 So. (Miss.) 112 (1888). In Dunham *v.* Schindler, 17 Ore. 256, 20 Pac. 326 (1889), the course pursued by plaintiff's attorney, in bringing an action against partners in the firm name, is spoken of as "discreditable to the profession." In Stout *v.* Baker, 32 Kan. 113, 4 Pac. 141) 1884), judgment was recovered against Stout and Wingert by their firm name, but each partner was served with process and appeared in the suit, and the court held both bound as individuals, as well as partners.

Neither partner, therefore, has a right to demand of the creditor, that he proceed against the firm assets, although they are ample, to satisfy his claim.[1] Nor can a debtor of either partner, when subjected to trustee process by a firm creditor, escape liability on the ground that his indebtedness is not to the firm, but to an individual partner.[2] In the language of the decision, last referred to, "As the debt due from the partners jointly is also due from each, it may be enforced against the separate property of each. It is immaterial whether this separate property is in the form of goods and movable chattels, or goods, effects, and credits intrusted and deposited in such a manner that they can only be attached upon a trustee process. It is not necessary that the principal debtors should have made a joint deposit, or that the fund should belong to them jointly. It is enough if funds attachable upon a trustee process are due from the alleged trustee to either one of the principal defendants."

The equitable rights of separate creditors, in the cases now under consideration, will be considered hereafter.

(*a*) *Statutory Modifications.* — The common law rule that actions against a firm must be brought against the partners by name, was often productive of inconvenience and prejudicial delay to creditors. To remedy this mischief, statutes have been enacted in many jurisdictions, permitting partnerships to be sued in the firm name.[3] It is inconsistent with the plan of this work to discuss these statutes; but, perhaps, this should be said, that none of them operate to turn the firm into a legal entity

[1] Hamsmith *v.* Espy, 13 Ia. 439 (1862); Burdick's Cases on Part. 376.

[2] Stevens *v.* Perry, 113 Mass. 380 (1873); Burdick's Cases on Part. 377.

[3] Hamsmith *v.* Espy, 13 Ia. 439 (1862); Stuart *v.* Corning, 32 Conn. 105 (1864); Lindley on Part. (6th ed.) 272.

for all purposes. "When a firm's name is used, it is only a convenient method for denoting those persons who compose the firm at the time when that name is used; and a plaintiff who sues partners in the name of their firm in truth sues them individually, just as much as if he had set out all their names."[1]

(*b*) *The Louisiana Doctrine.* — In Louisiana, the legal status of a partnership is quite different from that which is recognized by the common law. Under the jurisprudence of that State, "a partnership is a legal and moral entity, a civil person, with peculiar rights and attributes separate and distinct from the individuals composing it, . . . and while not capable of suing and being sued by itself, is capable of suing and being sued joined with the partners. When sued with the partners, and the plaintiff recovers, judgment is rendered against it and the partners individually." Nor is it necessary to join all of the partners as defendants with the firm, in case some of them are non-residents. Suit may be brought and judgment rendered against the firm and the resident members, even though the non-joinder of the non-resident partners is pleaded in defence.[2]

2. Attachment Proceedings. — These are the creatures of statutes, with different features in different jurisdictions. Notwithstanding their variations, however, the rules governing these proceedings, when instituted against partners, are not very divergent.

In the first place, the courts are generally agreed in holding that an attachment is a harsh and extraordinary remedy, and that a statute authorizing it should receive a strict construction, as being in derogation of the common law rights of debtors. It is likened[3] to the remedy of

[1] Lindley, L. J., in West. Nat. Bk. *v.* Perez [1891], 1 Q. B. 304, 314.

[2] Martin *v.* Meyer, 45 Fed. 435 (1891).

[3] Bogart *v.* Dart, 25 Hun (N. Y.), 395 (1881).

arrest in civil actions, which was briefly discussed in the last chapter.[1] It is intended as a remedy against a debtor who has been guilty of some misconduct, or whose non-residence would be productive of hardship to the creditor, were the latter confined to ordinary common law proceedings.

(*a*) *Partner's Misconduct outside Firm Affairs.* — Although this may be of such a nature as to authorize an attachment against his individual property, it will not warrant such a proceeding against the firm assets nor against the separate estate of his copartners. Accordingly, if firm creditors, in an action against all the partners on a firm debt, ask for an attachment because of the non-residence of one partner,[2] or because of the fraudulent transfer by one partner of his separate property,[3] the attachment will be limited to the property of the offending partner.[4] It is true, the attachment may be levied on the firm assets, but its lien will be confined to the interest of the offending partner, which, if the firm is then insolvent, is nothing.[5]

(*b*) *Partner's Misconduct in Connection with Firm Affairs.* — The transfer of firm property in fraud of its creditors will undoubtedly warrant an attachment against the firm and all of its members, when all have concurred in the act.[6] But suppose one partner, in an insolvent

[1] *Supra*, Chap. IV.

[2] Staats *v.* Bristow, 73 N. Y. 274 (1878).

[3] Evans *v.* Virgin, 69 Wis. 153; 33 N. W. 569 (1887).

[4] Williams *v.* Muthersbaugh, 29 Kan. 730 (1883), shows that, by reason of peculiar statutory provisions in that State, firm creditors can levy an attachment, issued against one partner only, on partnership property as a security for the firm debt. "To this extent the partnership must suffer for the individual wrongs of each of its members."

[5] Staats *v.* Bristow, 73 N. Y. 274 (1878); Andrews *v.* Mundy, 36 W. Va. 22; 14 S. E. 414 (1892).

[6] So if all the members are non-residents, an attachment may issue against firm property. Yerkes *v.* McFaddon, 141 N. Y. 136 (1896).

firm, without the knowledge or assent of his copartners, is applying partnership property to the payment of his individual debts, and thereby fraudulently withdrawing the property from firm creditors, can the latter obtain an attachment against the firm assets?

Keith *v.* Armstrong [1] is sometimes cited in support of an affirmative answer. But that case, as explained in a more recent opinion of the Wisconsin Supreme Court,[2] was decided on the ground that Armstrong, the fraudulent actor, was the managing partner, who was doing all the business of the firm, with his partner's consent, and that, therefore, his act was, in legal effect, the act of both. Clearly, Armstrong's use of the partnership assets, in paying his individual debts, was in excess of his implied authority as a partner, and but for the actual authority which the court declared had been given to him by his copartner, his attempted transfer could not operate to devest the firm title.[3] Unless his act was done with the consent of his copartner, it would not authorize an attachment against the firm and its property.[4]

(c) *Attachment against Innocent Partner's Property.* — A more difficult question is this: When one partner has committed an act, in the course of the partnership business, which entitles the creditor to an attachment against the firm, can the creditor levy the attachment on the separate property of the innocent partner? If the creditor brings an action for deceit against all the partners, he can recover damages against all, even though the deceit was practised by one without the knowledge or

Under the New York statute, the attachment can be levied, although service of the summons has been made on but one partner.

[1] 65 Wis. 225 (1886).

[2] Wimer *v.* Kuehn, 97 Wis. 394; 72 N. W. 227 (1897).

[3] *Supra,* Chap. III. § 3.

[4] Evans *v.* Virgin, 69 Wis. 148, 158; 33 N. W. 569 (1887).

assent of the others, provided the culpable partner was acting in the ordinary course of the business of the firm.[1] And having recovered judgment, he can levy his execution upon the separate property of any innocent partner.[2] It would seem to follow, therefore, that if an attachment may issue against the firm, in an action for deceit, it may be levied on the separate property of the partners as well as upon firm assets.

The Supreme Court of Michigan,[3] however, has held such a levy invalid, under the statutes of that State. In the opinion of the majority of the court, the statutory remedy of attachment is limited to the debtor who is guilty of the fraud, and its use is denied "against all honest persons, though they have the misfortune to be connected in business as partners with dishonest persons."[4]

### § 1. (A.) **Effect of Novation.**

While the right of a partnership creditor to sue the partners and to enforce his judgment against their separate property, as well as against the firm effects, cannot be impaired by the withdrawal of a partner, or by an agreement between the partners that one or more shall discharge the creditor's claim,[5] it may be lost by novation. The rule upon this subject has been formulated in a recent statute[6] as follows:

"A person who is admitted as a partner into an existing firm does not thereby become liable to the creditors of

[1] *Supra,* Chap. IV. § 2. Lindley on Part. (6th ed.) 161; British Part. Act of 1890, § 10.

[2] Randolph *v.* Daly, 13 N. J. Eq. 313, 316 (1863).

[3] Jaffray *v.* Jennings, 101 Mich. 515; 60 N. W. 52; 25 L. R. A. 645 (1894); Burdick's Cases on Part. 378.

[4] *Cf.* The dissenting opinion of Montgomery, J., in which McGrath, C. J., concurred, 101 Mich. 523–525.

[5] Briggs *v.* Briggs, 15 N. Y. 471 (1857).

[6] British Part. Act of 1890, § 17.

the firm for anything done before he becomes a partner. A partner who retires from a firm does not thereby cease to be liable for partnership debts or obligations incurred before his retirement. A retiring partner may be discharged from any existing liabilities by an agreement to that effect between himself and the members of the firm as newly constituted and the creditors, and this agreement may be either express or inferred as a fact from the course of dealing between the creditors and the firm as newly constituted.

(a) *Novation by Implied Agreement.* — In order to establish his discharge from a firm obligation, it is not necessary for the partner to prove an express agreement therefor, on the part of the creditor. It is enough for him to show "such facts, circumstances, acts, and conduct as would suffice to establish any other agreement or contract, in the absence of statutory provisions affecting the mode of execution or proof."[1]

Still the burden is upon the withdrawing partner to show that he has been discharged. He must plead and prove an agreement between himself, the firm, and the creditor.[2] It will not be presumed. On the other hand, "from the nature of the alleged agreement" — changing as it does established legal relations, and substituting a new security for an old one — "the absence of express words touching payment and release ought to weigh against its existence."[3] Mere silence of the creditor, when informed of an agreement between the partners that one has assumed, and is thereafter to be responsible for firm debts, will not establish his consent to the agreement nor make him a party thereto;[4] nor will the creditor's statement that he

[1] Bank *v.* Green, 40 Ohio St. 431 (1884).

[2] Benson *v.* Hadfield, 4 Hare, 32, 37 (1844).

[3] Bank *v.* Green, 40 Ohio St. 431, 440 (1884).

[4] Wadhams *v.* Page, 1 Wash. 420; 25 Pac. 462 (1890).

is aware he has no further claim on the retiring partner, have such effect.[1] Even the creditor's receipt of payments from the assuming partner or firm on account of the old firm's debt will not warrant the inference that he has contracted to discharge the retiring partner.[2] He has a right to receive payment from any partner, and such receipt would not be prejudicial to the one who has retired.[3]

(*b*) *New Security for Old Debt.* — Not only may a creditor allow a deposit, which he made with a firm, to remain in the custody of a partner or a new firm, after his or its assumption of the old firm's debts, and receive payments thereon, without discharging the retiring partner, but he may go further and receive the negotiable paper of the new firm or assuming partner, without releasing his hold upon his original debtors, provided he takes it simply as security for the old debt.[4] If it is given and received, however, with the intention to substitute it for the old firm's liability, the retiring partner will be discharged.[5] Such an intention appears clearly, when a bank depositor notifies the partner who continues the business of the bank after dissolution of the firm, that he wishes to withdraw his deposit for investment, and, upon the advice of the continuing partner, consents to leave it with him in a new account, upon terms radically different from those relating to the original account.[6]

(*c*) *Novation by Express Agreement.* — When the creditor has expressly agreed to substitute the liability of

[1] Kirwan *v.* Kirwan, 2 C. & M. 617 ; 4 Tyrwh. 491 (1834) ; Burdick's Cases on Part. 384.

[2] In re Head [1893], 3 Ch. 426 ; Burdick's Cases on Part. 387 *n.*

[3] Campbell *v.* Floyd, 153 Pa. St. 84, 95 ; 25 At. 1033, 1037 (1893); Harris *v.* Farrell, 13 Beav. 403 (1846).

[4] Smith *v.* Rogers, 17 Johns. (N. Y.) 340 (1820).

[5] Bank *v.* Green, 40 Ohio St. 431 (1884).

[6] In re Head [1894], 2 Ch. 236 ; Burdick's Cases on Part. 386.

one partner or of a new firm for that of the old partnership, the retiring partner is discharged, provided the agreement is made upon a legal consideration. If the new firm contains a member who was not in the old firm, or if a third person joins with the continuing partner in his promise to the creditor to pay the old firm debts, there can be no doubt that the creditor's agreement rests upon a legal consideration.

"The promise of a creditor," however, it has been said, "to release the outgoing and look to the continuing partners for payment, is not binding for want of consideration. The creditor had the several liability of the continuing partner already in the joint obligation." [1] But the weight of authority, both in England and in this country, is opposed to this view.

(*d*) *Assumption of Firm Debts by one Partner.* — In a leading case on this subject, Baron Parke gave the following reasons for holding such an agreement as we are now considering, binding on the creditors: "It cannot be doubted that the sole security of one of two joint debtors may be more beneficial than the joint responsibility of both. In the latter case, you are not entitled to sue one with safety, for the defendant may plead in abatement the non-joinder of his co-contractor. In the case of the bankruptcy of one of the partners, there would also be a difference. . . . Where there is more than one debtor, the creditor's right is different. There is, therefore, no doubt that the thing substituted is altogether different from the original debt." [2]

This is undoubtedly the better doctrine. The sole ob-

[1] Parsons (James), Principles of Part. § 95; Walstrom *v.* Hopkins, 103 Pa. 118 (1883); Early *v.* Burt, 68 Iowa, 716; 28 N. W. 35 (1886). In the last case it is said, the assuming partner's "undertaking was simply a promise to pay a debt for which he was already liable."

[2] Lyth *v.* Ault, 7 Exch. 669 (1852); Burdick's Cases on Part. 385.

ligation of one partner is a different thing from the obligation of the firm. If the creditor consents to substitute the former for the latter, the law will not inquire into the amount of the consideration for his promise, nor concern itself with the question whether his bargain is a good or a bad one.[1]

(e) *Novation by Estoppel.* — A creditor of a dissolved partnership, who has not agreed to discharge a retiring partner, may so conduct himself as to be estopped from proving his non-agreement. The case of Regester *v.* Dodge [2] may be referred to as an example.

Plaintiff's intestate was a creditor of Jay, Cooke, & Co. In 1871, Dodge withdrew, and a new firm was formed, composed of the remaining old members and two new ones, which assumed all the obligations. In 1873, the new firm went into bankruptcy, and in 1877 Dodge died. Plaintiff made no claim against Dodge during his life time; but in 1878 he demanded payment of the debt of Dodge's executor, who repudiated any liability. Plaintiff had proved his claim against the bankrupt firm, and upon the final settlement of that estate received certain stocks in lieu of money, which, without notice to Dodge's executor, he sold. After the final distribution of the bankrupt estate, plaintiff brought suit in equity against Dodge's executor for the balance of his claim. The court held that it would be inequitable for the plaintiff to maintain his suit after his conduct had not only indicated that he accepted the new firm as his debtor, in place of the old firm, but had deprived defendant of his right to take part in the bankruptcy proceedings and to receive and to dispose of the stocks which had been distributed to plaintiff.

1 Luddington *v.* Bell, 77 N. Y. 138 (1879); Allison *v.* Abendroth, 108 N. Y. 470; 15 N. E. 606 (1888); Parsons (T.) on Part. (4th ed.) § 240.

2 Regester *v.* Dodge, 19 Blatch. (U. S. C. C.) 79; 6 Fed. 6; 61 How. Pr. 107 (1881).

§ 1. (B.) **Effect of Judgment against one Partner.**

The common law doctrines that actions upon partnership obligations could not be brought against the firm, as an entity, but must be brought against the individuals composing the firm, and that such individuals were jointly — not jointly and severally — liable upon firm contracts, resulted in serious hardships to partnership creditors.

(*a*) *Non-Joinder must be Pleaded.* — The first improvement in the condition of firm creditors was effected by Lord Mansfield, who held that a creditor could recover against one or more partners, unless they pleaded in abatement the non-joinder of their associates, and thereby disclosed who the partners were.[1] "A creditor," said Lord Mansfield, "may be non-suited twenty times before he learns them all, or driven to a suit in equity for a discovery who they are. It is cruel to turn a creditor round, and make him pay the whole costs of a non-suit, in favor of a defendant who is certainly liable to pay his whole demand, and who is not injured by another partner's not being made defendant; because what he pays he must have credit for in his account with the partnership."

(*b*) *Absconding or Non-Resident Partners.* — But the woes of a firm creditor were not wholly cured by this doctrine of Lord Mansfield. After he had discovered all of the partners, there still remained the task, sometimes an arduous one, of compelling their appearance in the case, as a condition of his making further progress towards a judgment.[2] In case some of them were non-residents, he might resort to one of two methods, if his action was brought in a law court; he could distrain on firm property

[1] Rice *v.* Shute, 5 Burr. 2611; 2 W. Bl. 695 (1770); 1 Wm. Saund. 291 *a*, *n.* 4. If the non-joinder appears on the face of the complaint; a plea in abatement is unnecessary. Sandusky *v.* Sidwell, 173 Ill. 493; 50 N. E. 1003 (1898).

[2] Gow on Part. (2d ed.) 177.

if he could find any within the jurisdiction, or he could proceed to outlawry. As the former was the shorter and easier method, it was favored by the courts.[1] If he chose to go into a court of equity, he could file a bill against the resident partner and obtain a decree for the whole debt.[2]

In this country the process of outlawry has not been resorted to.[3] Some courts have held that the sheriff's return of *non est inventus*, as to one or more of the partners who are defendants, is sufficient to enable the creditor to proceed in his action against the other partners served with process.[4] Most of the States, however, have adopted statutes, called joint-debtor acts,[5] which are a substitute for the common law process of outlawry. By legislation of this character, the condition of a partnership creditor has been greatly improved. His failure to secure service of process upon all the members of a firm does not prevent his obtaining a judgment which can be enforced against the firm property as well as the separate property of the partners who were found and served.[6]

(c) *Merger of Firm Debt in a Judgment against one Partner.* — Perhaps the most grievous hardship imposed upon firm creditors by the common law doctrines, mentioned at the beginning of this section, was the absolute bar which a judgment against one or more of the partners interposed to a suit upon the same claim against the other partners. The rule upon this subject has been stated by a distinguished judge[7] as follows: "A judgment against

[1] Morley *v.* Strombone, 3 Bos. & P. 254 (1802).

[2] Darwent *v.* Walton, 2 Atk. 510 (1742).

[3] Nathanson *v.* Spitz, 19 R. I. 70; 31 At. 690 (1895); Burdick's Cases on Part. 393.

[4] Dillman *v.* Schultz, 5 S. & R. (Pa.) 35 (1819).

[5] Hall *v.* Lanning, 91 U. S. 160, 168 (1875).

[6] Stimson's Am. Statute L. § 5015. For some of the earliest American statutes, see Gow on Part. (2d Am. ed.) *179 (1).

[7] Field, J., in Mason *v.* Eldred, 6 Wall. (U. S.) 231 (1867); Burdick's Cases on Part. 388.

one upon a joint contract of several persons bars an action against the others, though the latter were dormant partners of the defendant in the original action, and this fact was unknown to the plaintiff when that action was commenced. When the contract is joint, and not joint and several, the entire cause of action is merged in the judgment. The joint liability of the parties not sued with those against whom the judgment is recovered, being extinguished, their entire liability is gone. They cannot be sued separately, for they have incurred no several obligations; they cannot be sued jointly with the others, because judgment has been already recovered against the latter, who would otherwise be subjected to two suits for the same cause."

(*d*) *Statutory Changes.* — The foregoing doctrine has been modified by legislation in many of our States. Some of the statutes go no further than regulating the effect of a judgment against a part of the partners which is taken in an action brought against all.[1] Others declare that every partner is jointly and severally liable with his copartners for all the obligations of the partnership.[2] The joint liability of partners is continued in England by the Partnership Act of 1890, § 9.

1. Liability of Partners for Partnership Torts. — This has always been several as well as joint.[3] Accordingly, if a part only are made defendants, they cannot compel the plaintiff to bring in the others;[4] nor will a judgment against one or more of the partners for the wrong be a bar, in this country, to a new action against

[1] See the Michigan statute which controlled the decision in Mason *v.* Eldred, *supra;* also Ohio statute referred to in Yoho *v.* McGovern, 42 Ohio St. 11 (1884).

[2] Stimson's Am. St. L. § 4113; Ch. 420, L. of 1897, N. Y.

[3] Rice *v.* Shute, 5 Burr. 2611 (1770); British Part. Act of 1890, §§ 11, 12.

[4] White *v.* Smith, 12 Rich. L. (S. C.) 595 (1860); Roberts *v.* Johnson, 58 N. Y. 613 (1874).

the others;[1] although, in England, a judgment against one of several joint wrongdoers, even when unsatisfied, is a bar to an action against the others.[2]

§ 1. (C.) **Remedies against Dormant Partners.**

The common law doctrine of merger operated necessarily to discharge a dormant partner, although his connection with the firm was unknown to the creditor when he took judgment against the ostensible partners.[3] No such consequence, however, attends upon those transactions between the creditor and the ostensible partners which do not work a merger of the creditor's claim against the firm.

For example, the creditor's right to sue the dormant partner, when discovered, is not affected by his having taken, in settlement of the firm debt, a bill of exchange drawn by the ostensible partner, although the bill is accepted by a third person;[4] nor by the creditor's taking a sealed note of the ostensible partner,[5] provided such paper is not paid. "It is clear law," said the courts, in the cases cited in the last two notes, "that a dormant partner cannot discharge himself from liability to pay the debts of a creditor, through the medium of his ostensible partner, by any acts of his during the concealment of the unknown partner."

1. Dormant Partner's Liability on Partnership Paper. — If he is a member of a trading partnership, his

[1] Lovejoy *v.* Murray, 3 Wall. (U. S.) 1 (1865); Burdick's Cases on Torts (2d ed.) 250.

[2] Brinsmead *v.* Harrison, L. R. 7 C. P. 547; 41 L. J. C. P. 190 (1872).

[3] Kendall *v.* Hamilton, 4 App. Cas. 504 (1879); Robertson *v.* Smith, 18 John. (N. Y.) 459 (1821).

[4] Robinson *v.* Williamson, 3 Price, 538 (1817); Burdick's Cases on Part. 396.

[5] Chamberlain *v.* Madden, 7 Rich. L. (S. C.) 395 (1854).

liability upon its negotiable paper is the same as that of the ostensible partners. When the business is carried on in the individual name of his copartner, who is also engaged in a separate business, the dormant partner will be liable on firm paper issued in that name.[1] He will also be liable as indorser on paper owned by the firm, indorsed in the firm name, and transferred to a *bona fide* holder. Under this doctrine, a bank which has discounted such paper for the partner who appears to be the sole owner of the business and of the paper, can recover against the dormant partner on the indorsement, although it did not know of the latter's connection with the business when it took the paper.[2]

(*a*) *The Doctrine of Swan* v. *Steele.* — In a leading English case[3] on this subject, it appeared that two partners carried on a grocery business in the name of Wood & Payne; at the same time they with Steele carried on the business of cotton dealers in the same firm name, Steele being a dormant partner therein. The grocery firm, being indebted to plaintiffs, gave them in payment a note payable to Wood & Payne and indorsed in that name. The note was not paid by the maker, and plaintiffs, discovering that the note was payable to the cotton firm, sued the members of that firm as indorsers. Steele pleaded *non assumpsit;* but judgment was given against him.

In the course of his opinion, Lord Ellenborough said: "Now here the three persons were trading under the firm of Wood & Payne, and in the course of their dealings as partners received the bill in question; and it was competent to either of them by his indorsement in the name of

[1] *Supra*, Chap. III. § 1.

[2] Mohawk Nat. Bank *v.* Van Slyck, 29 Hun (N. Y.), 188 (1883); Burdick's Cases on Part. 396.

[3] Swan *v.* Steele, 7 East, 210; 3 Smith, 199 (1806).

the firm to pass their interest in the bill; and the plaintiffs, ignorant of any fraud at the time, take it by such indorsement from one of the partners. Then, if the interest of the plaintiffs in the bill were once well vested, no subsequent knowledge that such indorsement was made without the consent of one of the partners will divest it." [1]

Nor, in such a case as the preceding, could the dormant partner, either in his own behalf or in behalf of the creditors of his firm, maintain an action to recover the paper from the plaintiffs. The dormant partner, having clothed the ostensible partners with authority to pass a perfect title to the paper, is estopped to set up the title of his firm against a *bona fide* purchaser.[2]

2. TERMINATION OF DORMANT PARTNER'S LIABILITY. — We have seen that an ostensible partner must give notice of his withdrawal from the firm, in order to absolve himself from liability for its subsequent obligations.[3] This duty does not rest upon a dormant partner. His connection with the firm has not increased its credit, for this connection was unknown. "There is no room, therefore, for the presumption that the public" will be "misled by the omission to give notice of the termination of the partnership." [4]

3. WHO IS A DORMANT PARTNER? — The authorities are not in accord upon this point. In England the term includes every member of the firm whose name does not appear in the firm style, and whose connection with the firm has not been known to the plaintiff.

[1] The true test of the dormant partner's liability in this class of cases has been stated as follows: "If a member of only one of the two firms is sued on the bill, his liability will depend, first, on the authority of the person giving the bill to use the name of the firm of which the defendant is a member; and, secondly, on whether the name of that firm has in fact been used." Lindley on Part. (6th ed.) 192.

[2] Kellogg *v.* Fancher, 23 Wis. 21 (1868).

[3] *Supra*, Chap. II. § 4.

[4] Kelley *v.* Hurlburt, 5 Cow. (N. Y.) 534 (1826).

The leading English case is that of Carter *v.* Whalley.[1] Four persons, the defendants in the action, had carried on a partnership under the name of the "The Plas Madoc Colliery Company;" but before plaintiff discounted the bill in suit for the partnership, Saunders, one of the partners, retired. No notice of his retirement, however, was given. Baron Parke said that in order to render Saunders liable on the ground of estoppel, it was necessary for the plaintiffs to show that he had been known to them as a member of the firm, either by direct transactions or by public notoriety. This, the plaintiff, he said, had failed to do. "The name of the company gave no information as to the parties composing it, and the plaintiffs did not show that Saunders had dealt with them in the character of a partner, or had held himself out so publicly to be one as that the plaintiffs must have known it."

The statutory provision upon the subject is as follows: "The estate of a partner who dies, or who becomes bankrupt, or of a partner who, not having been known to the person dealing with the firm to be a partner, retires from the firm, is not liable for partnership debts contracted after the date of the death, bankruptcy, or retirement, respectively."[2]

Under this rule, if the partnership remains perfectly secret, the dormant partner will not be affected by partnership transactions after his withdrawal, "but if the partnership had become known to any person or persons, he would be in the same situation, as to all such persons, as if the existence of the partnership had been notorious."[3]

(*a*) *Dormancy Involves Inactivity as well as Secrecy.* — While the foregoing doctrine of the English courts and

[1] 1 Barn. & Ad. 11 (1830).

[2] British Part. Act, § 36 (3).

[3] Farrar *v.* Deflinne, 1 Car. & K. 580 (1843); Lieb *v.* Craddock, 87 Ky. 525; 9 S. W. 838 (1888).

statute has been adopted in some of our States,[1] in others it is held that "a dormant partner is one who takes no part in the business, and whose connection with it is unknown. Both secrecy and inactivity are implied by the word."[2]

Accordingly, though a particular partner's name may not appear in the firm style, and though he may not have been known to a particular dealer or to the public as a partner, yet, if he has been an active member of the firm, he must give due notice of his withdrawal to former customers, if he would effectually terminate his liability for its subsequent obligations to them.[3] In the last cited case, the court said: "It was not necessary that the plaintiffs should have known the names of the defendants. They might, from their own experience and otherwise, have become satisfied that the Spring Brook Mills Company (the firm name of defendants) contained, and was managed by persons, as members of the firm, who were men of means, as well as regular and prompt in paying all their debts, although they never had ascertained the names of such persons. . . . It could not properly be ruled, as matter of law, that the defendants owed no duty of giving notice to the plaintiffs of their withdrawal from the firm, merely because the plaintiffs did not know that these individuals were the responsible parties in the firm."

(*b*) *Other Authorities for this View.* — This view has received the approval of the courts of last resort of Pennsylvania[4] and New York,[5] in two very carefully considered

[1] Austin *v.* Appling, 88 Ga. 54; 13 S. E. 955 (1891). In the latter State, the statutory provision is quite similar to that in the British Part. Act.

[2] Nat. Bank of Salem *v.* Thomas, 47 N. Y. 15, 19 (1871).

[3] Elkinton *v.* Booth, 143 Mass. 479; 10 N. E. 460 (1887).

[4] Shamburg *v.* Ruggles, 83 Pa. St. 148 (1876).

[5] Elmira Iron Co. *v* Harris, 124 N. Y. 280; 26 N. E. 541 (1891); Burdick's Cases on Part. 398.

cases. In the opinion of these tribunals, when a business is carried on, not in an individual's name, but in a name which indicates a partnership, it is not only fair to presume that credit has been given upon the reputation of the firm, rather than upon the names of the individuals composing it, but such presumption is supported by modern business methods. In the language of the New York court: "The inquiry addressed naturally is, what is the financial condition of Jones & Co.? For having no acquaintance with the individuals comprising the firm, information as to membership does not aid the inquirer."

(c) *Notice to the Public Unnecessary.* — While a secret but active partner is bound to give notice of his withdrawal to former customers under the rule last stated, he owes no such duty to those who have never dealt with the firm during his connection with it. To such persons, it has been judicially declared, "He will not be liable even though no notice of dissolution of any kind be given, unless he does some act or acts, or permits or suffers acts or things to be done, which would lead such persons, having knowledge thereof, to believe that the firm continued to exist at the time of their dealing with the other partners on the credit of such firm."[1]

## § 2. Remedies of Separate Creditors at Law.

So long as the separate creditors of a partner confine their attempts to enforce legal process to his individual property, no serious legal difficulties are encountered. The lien of their judgment or levy will depend upon its priority. To the vigilant and not to the sleepy creditor does the common law give its reward of merit, and it does not inquire whether he is a partnership or a separate creditor. But quite different principles are applied when the separate creditor undertakes to enforce his common law process

[1] Benjamin *v.* Covert, 47 Wis. 375, 385; 2 N. W. 625 (1879).

against his debtor's interest in partnership property; and the situation often becomes painfully complicated.

1. The Value of his Judgment Lien Uncertain. — We have seen that a partner has no individual title to any of the firm assets; that his interest is but a chose in action — a right to a share of what remains after the partnership debts are paid and the equities of the partners are adjusted.[1]

Hence, a separate creditor may secure the levy of his execution on firm assets which are worth ten times the amount of his judgment, this, too, before any other judgment or execution lien has attached; and yet he may not realize a cent as the fruits of his diligence. If, at any time before a sale under his process, firm creditors issue valid executions to the sheriff sufficient to exhaust the firm property, the separate creditor's executions must be returned *nulla bona*.[2]

2. Partnership Property is Seizable under Separate Execution. — Under the doctrine established by the common law courts in England, the sheriff levied a separate creditor's execution by seizing a part or all of the tangible property of the firm. In no other way, it was thought, could the levy be made effectual, the shares of the two partners being undivided.[3] This practice has been followed generally by the law courts of this country. In some jurisdictions, however, a constructive levy only is permitted; and actual seizure and removal of specific chattels of a partnership, under attachment or execution against one member, are deemed a trespass.[4]

[1] *Supra*, Chap III. § 3.

[2] Eighth Nat. Bank *v.* Fitch, 49 N. Y. 539 (1872); Burdick's Cases on Part. 403. In Hacker *v.* Johnson, 66 Me. 21, 25 (1877), it is said that the execution creditor is entitled to a sale of the debtor partner's interest, for it may sell for something whether the firm is insolvent or not.

[3] Johnson *v.* Evans, 7 Man. & Gr. 240 (1844).

[4] Sanborn *v.* Rice, 132 Mass. 594 (1882).

Even the jurisdictions which permit actual seizure of firm assets, in levying an individual execution, are not agreed as to whether the sheriff must seize all of the tangible property of the firm, or may seize a part only. In favor of the former view, it is said: "In an action against one of the partners, the officer must seize all the goods, because the moieties are undivided; for if he seize but a moiety and sell that, the other partners will have a right to a moiety of that moiety. He must seize the entire leviable property of the copartnership. He must take and retain custody of the property, for in no other way can he legally execute the writ and sell as much of the interest of his judgment debtor as may be sufficient to satisfy the execution."[1]

(*a*) *Execution may be Levied on Specific Chattels.*— On the other hand, it is argued that to require a levy upon all the partnership effects, however small the judgment, is to impose an unnecessary duty upon the individual creditor and an unnecessary hardship upon the firm. The debtor's interest in the entire property might be greatly in excess of what was required to satisfy the execution. Again, the firm assets might be situated in various jurisdictions, and a levy upon all of them might be impossible.[2]

3. Execution Creditor's Rights after a Levy.— While the separate creditor can have his execution levied on firm assets, at common law, he does not acquire thereby

[1] Branch *v.* Wiseman, 51 Ind. 1, 3 (1875), following Heydon *v.* Heydon, 1 Salk. 392 (1693). In Wigham's Appeal, 63 Pa. 194, 198 (1869), Sharswood, J., said: "Partners have no separate title in any aliquot part of the partnership property. Their interest is an incorporeal, intangible thing, a right to an account, and to their share of the balance after all the partnership debts are paid and all the equities between the partners adjusted. If, upon an execution against one partner, the sheriff should levy upon and sell his interest in a single bale of goods, it could not be maintained that his vendee would acquire his interest in all the assets."

[2] Fogg *v.* Lawry, 68 Me. 78 (1878).

any legal interest in such assets. Accordingly, if the firm goes into bankruptcy,[1] or makes an assignment for the benefit of creditors,[2] after the levy, the title to the assets will pass to the assignees, who may dispose of them free from the lien of the levy; and, if the firm is insolvent, free from any liability to pay to the execution creditor any part of the proceeds.

4. THE SHERIFF'S RIGHTS AFTER A LEVY. — According to the old English cases, the sheriff laid hold of any firm chattels which he could find, and sold the debtor partner's interest therein, as though it were the share of a tenant in common, and paid the proceeds over to the execution creditor.[3] Later, however, it was held that the sheriff had no right to take the goods of the firm out of the possession of the solvent partners,[4] although, in order to make an effective levy, he could seize them.

But in American jurisdictions, where an actual levy is authorized, the sheriff is permitted to take actual and exclusive possession of the firm property.[5] "For what purpose," said Judge Cowen, in the case last cited, "does a sheriff seize property on a *fi. fa.* if not to remove and sell it? . . . Is the law so absurd as to command a sheriff by its writ to seize and sell an article, yet forbid him to remove it, or declare him a breaker of the peace for selling it, because he was resisted, and put to the exercise of force? This is a sort of imbecility which the common law has been careful to avoid in all cases."

Still, even in these jurisdictions, it is admitted that the rights of the execution creditor and of the sheriff are sub-

[1] Garbett *v.* Veale, 5 Q. B. 408; 13 L. J. Q. B. 98 (1843).

[2] Staats *v.* Bristow, 73 N. Y. 264 (1878).

[3] See Lord Eldon's account of the old cases in Dutton *v.* Morrison, 17 Ves. 193 (1810).

[4] Patterson, J., in Burnett *v.* Hunt, 5 Jur. 650, 651 (1841).

[5] Phillips *v.* Cook, 24 Wend. (N. Y.) 389, 393, 394 (1840).

ordinate to those of the other partners, and of the firm creditors "to have the property applied in payment of the partnership debts, if necessary for that purpose."[1] Hence, although the solvent partners cannot maintain replevin against the sheriff who seizes and removes firm assets under legal process against one of their associates,[2] and may subject themselves to an action for damages if they retake the property from the sheriff;[3] yet, if they can show that all the property levied on was needed for firm debts, damages will be nominal, and a purchaser from the sheriff under such an execution will get nothing by his purchase.[4]

(*a*) *Sheriff may be Liable in Tort.* — Moreover, if the sheriff removes the property and undertakes to transfer the entire title thereto, instead of selling merely the debtor's interest therein, he will be guilty of conversion.[5]

5. The Rights of the Purchaser. — Under the old English cases above referred to,[6] the purchaser became a true tenant in common with the solvent partner in the particular chattel sold by the sheriff. Lord Mansfield introduced a change, which has been described as follows: "The sheriff seized and sold the whole of a sufficient portion of the partnership goods, . . . and then an account was directed to be taken of the judgment debtor's share of the proceeds of the sale, and that share, or a sufficient part of it, was handed over to the execution creditor."[7] This innovation was discontinued because a

[1] Eighth Nat. Bank *v.* Fitch, 49 N. Y. 539 (1872); Burdick's Cases on Part. 403, 404.

[2] Smith *v.* Orser, 42 N. Y. 132 (1870).

[3] Haskins *v.* Everett, 4 Sneed (Tenn.), 531 (1857).

[4] ~~Johnson *v.*~~ Wingfield (Tenn.), 42 S. W. 203 (1897).

[5] Daniel *v.* Owens, 70 Ala. 297, 302 (1881); Michalover *v.* Moses, 19 App. Div. (N. Y.) 343 (1897); Burdick's Cases on Part. 417.

[6] Heydon *v.* Heydon, 1 Salk. 392 (1693), is an example.

[7] Lindley on Part. (5th ed.) 357.

law court could not conduct a partnership accounting, and therefore could not do full justice to the parties. Thereafter, until the adoption of the Partnership Act of 1890, the English practice was for the sheriff to sell the debtor partner's interest in the goods levied upon, making the purchaser a quasi tenant in common, and leaving him to ascertain as best he might what interest he had acquired.[1]

Such, in the main, has been the practice of the law courts in this country. Under this practice, the purchaser did not become the owner of any chattels, nor even a true tenant in common of any chattels. He acquired "a mere right in equity to call for an account, and thus to entitle himself to the interest of the partner in the property, which may be ascertained to exist upon a settlement, which may be something or nothing."[2]

6. Resort to Equity. — In England, and in some American jurisdictions, the debtor partner or his solvent associates, in such circumstances as we have been considering, can obtain relief in a court of equity. He is allowed to maintain a suit, to which all the partners and the creditor are parties, for a partnership accounting, the appointment of a receiver, and an injunction restraining the sheriff from selling the debtor's uncertain interest in the property.[3] Equity intervenes for the purpose of preventing a multiplicity of suits, of securing the unquestionable lien of the solvent partners, and of preventing a needless sacrifice of the debtor partner's interest by compelling a sale of it at a time when its value is wholly problematical.[4]

[1] Holmes *v.* Mentze, 4 A. & E. 127 (1835).

[2] Farley *v.* Moog, 79 Ala. 148, 153 (1885); Johnson *v.* Wingfield, 42 S. W. 203 (1897); Burdick's Cases on Part. 406; Lane *v.* Lenfest, 40 Minn. 375 (1889).

[3] Bevan *v.* Lewis, 1 Sim. 376 (1827); Place *v.* Sweetzer, 16 Ohio, 142 (1847).

[4] Story on Part. (7th ed.) § 264.

In other jurisdictions, equity has declined to intervene, partly because of a lack of precedent, partly because it is thought that, as the execution sale must be made subject to the rights of partnership creditors, no harm is done to them by the sale, and partly because it is said, the principle of enjoining the sale "would go to stay executions at law in every case against the partnership property of one partner, who owed separate debts, until the disclosure and liquidation of the concerns of the copartnership."[1]

7. GARNISHMENT OF DEBTS DUE THE FIRM. — It is generally held that a creditor of one partner cannot maintain garnishment proceedings against the debtor of the firm. These statutory proceedings have been treated by the courts as legal and not equitable in their nature, and the rights, credits, and effects which may be reached by them[2] "in the hands of the garnishee, are such as are not incumbered with trusts, and such as may be delivered over, or paid by the officer under the direction of the court, free from incumbrances. . . . It was not contemplated by the Legislature to authorize a court of law, in a mere side issue growing out of an attachment suit, to exercise the intricate and complicated duties of a chancellor," nor to compel the garnishee "to await the determination of a chancery proceeding requiring an adjustment of accounts between parties and partnerships."

8. STATUTORY MODIFICATIONS OF COMMON LAW PROCEDURE. — The evils[3] consequent upon the common law

[1] Moody *v.* Paine, 2 Johns. Ch. 548 (1817); 3 Kent's Comm. (14th ed.) 65, note *b*.

[2] Sheedy *v.* Sec. Nat. Bank, 62 Mo. 17 (1876); 21 Am. R. 407; *contra*, Thompson *v.* Lewis, 34 Me. 167 (1852).

[3] In Trafford *v.* Hubbard, 15 R. I. 326 (1886), it is said: "Undoubtedly this (the exclusive possession of the sheriff under a levy) tends to embarrass and possibly to break up the copartnership business; but we do not see how these consequences can be avoided at law, even if they can in equity, without remedial legislation."

methods of enforcing the judgments of separate creditors against firm property have been remedied to a greater or less extent by legislation.

For example, in New York, the partners other than the judgment debtor may get rid of the sheriff upon due application to the court, by giving an undertaking that they will account to the purchaser of the debtor partner's interest in the property seized, and pay to him the balance due the partner on such accounting, as they would be bound to do to an assignee of such interest.[1]

In Kentucky, the sheriff is forbidden to deprive the other partners of the possession of the property, except for the purpose of having it inventoried and appraised; and upon the officer's return of the inventory and appraisement with a statement of the claim of the other partners, the creditor may enforce the lien acquired under the levy, by an action in equity.[2] If in such action it appears that the debtor partner had no interest in the property levied on, because of the insolvency of the firm, or for any other reason, the creditor will take nothing by his action.[3]

(*a*) *Separate Creditor Prohibited from Levying on Firm Property.*—The Georgia Code declares that "the interest of a partner in the partnership assets may be reached by a judgment creditor by process of garnishment served on the firm, and shall not be subject to levy and sale."[4] After the service of the process of garnishment, the firm answers, and the issue thus raised as to the interest of the debtor partner in the firm is submitted to a jury, upon

[1] N. Y. Code of Civ. Proc. §§ 1413 to 1417. Others sections provide for the release of firm property from attachment by a separate creditor, §§ 693 to 696.

[2] Kentucky Civil Code of Prac. § 660.

[3] Holmes *v.* Miller, 41 S. W. (Ky.) 432 (1897); Burdick's Cases on Part. 417.

[4] Code of the State of Ga. (1895) § 2661; Willis *v.* Henderson, 43 Ga. 325 (1871); Burdick's Cases on Part. 418.

whose verdict judgment is entered for the creditor, in case it is shown that the debtor will be entitled to a share in the firm property after settlement of its affairs; otherwise judgment passes against the creditor.[1]

(*b*) *Statutory Change in Britain.* — By the British Partnership Act, a still more radical change has been made in the methods of enforcing a separate creditor's judgment against firm property. The issue of an execution on such a judgment against any partnership property is prohibited; and the creditor is authorized to apply for an order charging the debtor partner's interest in the partnership property and profits with the payment of his judgment with interest. The court may also appoint a receiver of such interest, and may "direct all accounts and inquiries, and give all other directions which might have been directed or given if the charge had been made in favor of the judgment creditor by the partner, or which the circumstances of the case may require."[2]

9. Right of Judgment Creditor or Purchaser to an Account. — The purchaser of the debtor partner's interest in the firm property under a separate creditor's execution, does not become a partner in the debtor's stead. The doctrine of *delectus personarum* prevents such a result. Having acquired the partner's interest, however, courts of equity, even in jurisdictions which do not accord an accounting to the judgment creditor before sale under his execution, permit him to call the solvent partners to an accounting, in order that he may receive the distributive share which he has bought.[3] Nor will

1 Code of the State of Ga. (1895) §§ 4705–4729; Armand *v.* Burrun Company, 69 Ga. 758 (1882).

2 Partnership Act of 1890, §23. "It is no secret that the present amendment of the law is due to the counsels of Lord Justice Lindley." Pollock's Dig. of Part. (6th ed.) 71.

3 Eighth Nat. Bank *v.* Fitch, 49 N. Y. 539 (1872); Burdick's Cases on Part. 403, 405.

his action for an accounting be defeated by the fact that the only partnership assets consist of a stock of goods of which he has an inventory.[1] The sale of the debtor partner's interest, according to the prevailing view in this country, works a dissolution of the partnership, and entitles the purchaser to ask for a final settlement and adjustment of the partnership affairs.[2]

If the sale has been made under a levy upon a part only of the firm effects, the debtor partner as well as the other members of the firm must be made parties.[3] Indeed, in such a case, the debtor partner would have the right to institute an action for an accounting, for he has not been completely divested of his interest in the firm.[4]

When a part only of the partnership assets is levied upon and sold, the mode of determining what interest has been acquired by the purchaser "is to take an account in equity of the other assets and of the debts of the firm, and in case the firm debts are paid from the other assets, the purchaser will be entitled to the execution debtor's proportion of the property purchased, as in what should remain after payment of such debts."[5]

(*a*) *The Present English Doctrine.* — Prior to the Partnership Act, the right of a purchaser of a partner's share to call the other partners to an account, had been judicially upheld, and had been judicially denied. All doubt upon the subject has been removed by that Act. Sections 23 and 31 deny to the separate creditors, or to any assignee of a partner's share, the right to interfere in the management or administration of the partnership,

1 Marx *v.* Goodnough, 23 Ore. 545 ; 32 Pac. 511 (1893).

2 Miller *v.* Brigham, 50 Cal. 615 (1875).

3 Gerard *v.* Bates, 124 Ill. 150; 16 N. E. 258 (1888).

4 Habersham *v.* Blurton, 1 De G. & S. 121 (1847), and preceding note.

5 Eighth Nat. Bank *v.* Fitch, 49 N. Y. 539 (1872) ; Burdick's Cases on Part. 403, 405.

during its continuance, or to require any accounts or to inspect the books. He is, indeed, entitled to the share of profits of the debtor or assigning partner, but "must accept the account of profits agreed to by the partners." Nor does the assignment of a partner's share necessarily dissolve the firm; although it gives the other partners a right to apply for a decree of dissolution;[1] and if a partner suffers his share to be charged under § 23, the partnership may be dissolved at the option of the other partners.[2]

The Act also provides that the other partners may redeem the debtor partner's interest, or, in case a sale of it is ordered by the court, they may purchase it.[3] If they avail themselves of this privilege, they must act with the utmost good faith towards the debtor partner;[4] and if they pay for the share with partnership funds, they do not become its owners, nor thereby cut off the debtor partner from membership in the firm with a partner's right to an accounting from them.[5]

10. Specific Legal Liens. — In the next section, it will appear that the relative rights of firm creditors and of separate creditors, with respect to the separate estate of a partner, are quite different, when the firm and separate estates have been brought within the jurisdiction of courts

[1] Partnership Act of 1890, § 35.

[2] Partnership Act of 1890, § 33 (2); see Brown, Janson, & Co. *v.* Hutchinson & Co. [1895] 2 Q. B. 126; Burdick's Cases on Part. 419, for the present English doctrine.

[3] Partnership Act of 1890, § 23 (3).

[4] Perens *v.* Johnson, 3 Sm. & G. 419 (1857). The solvent partners in a coal mine, before the sale of the debtor partner's interest by the sheriff, prevented access to the coal mine, so as to prevent this partner or bidders from knowing that the seam of coal was almost reached, and then bid in his interest for themselves. They were held to be trustees of the share for the debtor partner who had thus been overreached.

[5] Helmore *v.* Smith, 35 Ch. D. 436 (1887).

of equity, from the rights which are enforced in the courts of common law. Still, if the firm creditor has obtained a specific legal lien on a partner's separate estate, before the separate creditor has brought that estate under equity jurisdiction, the latter must abide the consequences of his tardiness. Accordingly, the absolute lien on a partner's real estate of a judgment in favor of a firm creditor,[1] or on his personal property under the levy of a firm creditor's execution,[2] cannot be destroyed or affected by proceedings subsequently instituted in a court possessing equity powers and administering the two estates under equity rules. Such courts never set aside or interfere with "an absolute right of priority obtained at law."

### § 3. The Rights of Creditors in Equity.

In administering the partnership estate and the separate estates of the partners which have been brought within its jurisdiction, a court of equity proceeds upon different principles from those which we have found to obtain in courts of law.

1. THE VIGILANT CREDITOR CANNOT GAIN A PREFERENCE. — As soon as a court of equity acquires jurisdiction of the property, the race between creditors for precedence is at an end. It does not matter whether this jurisdiction is obtained by an assignment in trust for the benefit of creditors, or by a petition in bankruptcy, or by a bill for the adjustment of the affairs of an insolvent partnership: in each case, further contest between creditors for advan-

[1] Meech *v.* Allen, 17 N. Y. 300 (1858).

[2] In re Sandusky, 17 N. B. R. 452 (1878); Burdick's Cases on Part. 421. In the two last cited cases, it is intimated that equity may interfere if the separate creditor shows that there is sufficient partnership property, subject to the firm creditor's lien, to satisfy his claim, while if he enforces it against the separate estate, the separate creditor will not be able to collect his debt. See U. S. Bankruptcy Act of July 1, 1898, § 67 (*d*).

tage of position is bootless. Specific legal liens, which have been acquired before equity obtains jurisdiction, will, as we saw in the last section, be respected; but from the moment jurisdiction is obtained the rule of equal distribution between creditors of the same class is enforced.

Hence, if an equity action is brought by one partner against the others, for the purpose of winding up the affairs of an insolvent partnership, the receiver, who is appointed therein, can hold the firm property, free from judgments thereafter obtained by partnership creditors.[1]

2. Firm Creditors Restricted to Firm Estate. — We have seen that a firm creditor at law could levy his execution upon the firm assets, or upon the separate property of a partner, at his option; and that if he obtained a lien on the separate property, he could enforce it, although he thereby exhausted this estate and left the separate creditor with a claim against a penniless debtor.

A different doctrine was established in equity, at an early day. It is stated as follows in a decree by Lord Chancellor Cowper, in one of the first reported cases upon the subject: "That, as the joint or partnership estate was in the first place to be applied to pay the joint or partnership debts, so in like manner the separate estate should be in the first place to pay all the separate debts: and as separate creditors are not to be let in upon the joint estate, until all the joint debts are paid; so likewise the creditors to the partnership shall not come in, for any deficiency of the joint estate, upon the separate estate, until the separate debts are first paid."[2]

[1] Holmes v. McDowell, 15 Hun (N. Y.), 585 (1878); Burdick's Cases on Part. 434. But if the firm is solvent, the partners cannot thus hold their creditors at bay, by an equity action and the appointment of a receiver. Matter of Thompson, 10 App. Div. (N. Y.) 40 (1896).

[2] Ex parte Crowder, 2 Vern. 706 (1715).

This doctrine has been embodied in the Bankruptcy Statutes of England[1] and of this country. The provision of the United States bankruptcy law of 1898 upon this topic reads as follows: "The trustee shall keep separate accounts of the partnership property and of the property belonging to the individual partners. The expenses shall be paid from the partnership property and the individual property in such proportions as the court shall determine. The net proceeds of the partnership property shall be appropriated to the payment of the partnership debts, and the net proceeds of the individual estate of each partner to the payment of his individual debts. Should any surplus remain of the property of any partner after paying his individual debts, such surplus shall be added to the partnership assets and be applied to the payment of the partnership debts. Should any surplus of the partnership property remain after paying the partnership debts, such surplus shall be added to the assets of the individual partners in the proportion of their respective interests in the partnership."[2]

(*a*) *The Doctrine Not Universally Accepted.* — Although this doctrine has long been the prevailing one, it was repudiated in England by Lord Thurlow, so far as the limitation it imposed on the firm creditor's right is concerned; he holding that a creditor of the firm is a creditor of each partner and entitled to share *pari passu* with the separate creditors in the separate estate.[3] This view was rejected in turn by Lord Rosslyn, who declared that a bankruptcy proceeding against a partner was not to be treated as an execution at law, but that the effects of the bankrupt were to be administered according to equitable rules, one of which was "that each estate is to pay

[1] Bankruptcy Act of 1883, §§ 43, 59.

[2] U. S. Bankruptcy Act of July 1, 1898, § 5 (*d*), (*e*), and (*f*).

[3] Ex parte Copland, 1 Cox Eq. 420 (1787).

its own creditors."[1] Lord Eldon, while expressing his preference[2] for Lord Thurlow's rule, declined to unsettle the rule adopted by the earliest cases and restored by his immediate predecessor.[3] This he did, not because he looked upon such rule as the best in principle, nor as founded upon any clear principle of equity,[4] but as one which had originated and was to be maintained upon considerations of convenience.[5]

(*b*) *Lord Thurlow's Rule in this Country.* — The rule laid down by Lord Thurlow has been preferred by several courts of last resort in this country. A well considered case of this class is that of Camp *v.* Grant.[6] In answer to the charge that if a court of equity, while devoting the firm property in the first instance to firm creditors, does not secure to separate creditors a like preference in the separate estate of the partners, it gives an advantage to firm creditors over separate creditors, the majority of the court said: "This is so: but it is no other advantage than what appertains to a creditor having two securities over another creditor who has but one. . . . The inequality or advantage does not grow out of an unequal application of a rule of equity, but out of the nature of the debt and property in question."

(*c*) *Modifications of Lord Thurlow's Rule.* — In Vermont[7] and South Carolina,[8] it is held that equity ought not

1 Ex parte Elton, 3 Ves. Jr. 238 (1796).

2 Ex parte Hill, 2 Bos. & P. 191, note *a* (1802).

3 Ex parte Kensington and Taylor, 14 Ves. 447 (1808).

4 Gray *v.* Chiswell, 9 Ves. 118, 126 (1803).

5 Dutton *v.* Morrison, 17 Ves. 193 (1810).

6 21 Conn. 41 (1851).

7 Bordwell *v.* Perry, 19 Vt. 292 (1847).

8 Hutzler Bros. *v.* Phillips, 26 S. C. 136; 1 S. E. 502 (1886). In Kentucky, "If the partnership creditors exhaust the partnership assets without being paid in full, the individual creditor has the right to make a like amount out of the individual assets, and when this is

to interfere, in such cases as we are now considering, beyond the point of requiring the firm creditors to confine themselves to the firm property in the first instance. After this is exhausted, the firm creditors should be allowed to share *pari passu* with the separate creditors in the whole of each separate estate. The prevailing doctrine in equity, which gives a preference to separate creditors in the separate estate, is declared by the Vermont Court to rest either "upon the mere ground of the English bankrupt laws, or else upon the mistaken ground, that a partnership creditor has no separate and entire claim upon the individual responsibility of each partner, for his whole debt."[1] Similar decisions have been made in Louisiana and Virginia, based in part upon statutory provisions.[2]

(*d*) *The Prevailing Rule Empirical.* — As early as 1728, the rule was characterized by Lord Chancellor King as "a resolution of convenience,"[3] and a modern English judge has spoken of it as belonging to "a sort of rough code of justice," established "because some rule must be laid down for the purpose of keeping joint and separate estates distinct, and for paying the joint and separate creditors."[4] Sir Frederick Pollock remarks that this and other "rules of administration between the creditors of the firm and the separate creditors of the partners have been settled and adhered to after much hesitation in the earlier cases . . . as an empirical way of dealing with a

done, the individual estate remaining will be distributed among all the creditors (partnership and individual) in proportion to their respective debts." Fayette Nat. Bank *v.* Kenney, 79 Ky. 133, 140 (1880).

[1] This view is approved in Story on Part. (7th ed.) §§ 376, 377; while Chancellor Kent upholds the prevailing rule as "upon the whole reasonable and just." 3 Kent's Comms. (14th ed.) *65 note (*b*).

[2] Guéringer *v.* His Creditors, 33 La. Ann. 1279 (1881); Pettyjohn *v.* Woodruff, 86 Va. 478; 10 S. E. 715 (1890).

[3] Ex parte Cook, 2 P. W. 500 (1728).

[4] Lord Justice James, in Lacey *v.* Hill, L. R. 8 Ch. 441, 444 (1872).

pressing necessity, rather than as being reasonable in themselves."[1]

This characterization of the rule is undoubtedly correct, and yet many learned judges both in this country and in England have undertaken to sustain it, not simply as an established rule and one which works fairly well, but as a rule which accords with equitable principles.[2]

(*e*) *Exceptions to the above Rule.* — The courts have found it necessary to establish some exceptions to the foregoing rule. These will be considered at length in the next two sections, in connection with various corollaries from the rule, inasmuch as they are applied in the same way by courts of bankruptcy and by equity tribunals.

3. The Rights of Secured Creditors. — Upon this topic, bankruptcy statutes, generally, have not followed the principles which have been established in equity. According to these principles, a creditor who has obtained from his debtor specific security for the debt is entitled to prove against the debtor's estate, when brought into equity for distribution, the full amount of his claim, and to receive a dividend on that amount. He may also enforce his security. If the latter produces more than is needed to pay the balance due on the claim, after the application of the dividend, the surplus belongs to the debtor's estate, and is distributable among the other creditors.[3]

[1] Pollock's Digest of Part. (6th ed.) 146.

[2] Rodgers *v.* Meranda, 7 Ohio St. 179 (1857); Burdick's Cases on Part. 424; Davis *v.* Howell, 33 N. J. Eq. 72 (1880); Burdick's Cases on Part. 438.

[3] People *v.* E. Remington & Sons, 121 N. Y. 328; 24 N. E. 793 (1890); Burdick's Cases on Part. 442. *Contra*, Amory *v.* Francis, 16 Mass. 308 (1820), following the English bankruptcy rule; Wurtz *v.* Hart, 13 Iowa, 515 (1862). In Third Nat. Bank *v.* Lanahan, 66 Md. 461 (1886), it was held that if the secured creditor has realized on his security, before a dividend is declared, he is entitled to a dividend on the balance only of his claim.

This result accords with the contract between the debtor and creditor, and with the general rule of equity that "the creditor is not bound to apply his collateral securities before enforcing his direct remedies agains the debtor."

(*a*) *The Bankruptcy Rule.* — If the debtor's estate has been brought within a bankruptcy court for distribution, the creditor who holds a security on such estate finds himself subject to a different rule from that which prevails in equity. "The principle of the bankrupt laws is, that all creditors are to be put on an equal footing, and therefore, if a creditor chooses to prove under the commission, he must sell or surrender whatever property he holds belonging to the bankrupt."[1]

This rule has been embodied in our present Federal Bankruptcy Law, which provides that "The value of securities held by secured creditors shall be determined by converting the same into money according to the terms of the agreement pursuant to which such securities were delivered to such creditors or by such creditors and the trustees, by agreement, arbitration, compromise, or litigation as the court may direct, and the amount of such value shall be credited upon such claims, and a dividend shall be paid only upon the unpaid balance."[2]

If the security equals or exceeds the debt, the creditor, of course, has no need to prove his claim; and any surplus in his hands after satisfying his claim will belong to the bankrupt's estate. If, however, he proves his claim at all, he must state under oath what securities he holds therefor.[3]

(*b*) *Creditors Secured by Third Persons.*—Neither in

[1] In re Plummer, 1 Phillips, 56 (1841); Burdick's Cases on Part. 444, note; British Bankruptcy Act of 1883, § 39, and Schedule 2, rules 9 to 17.

[2] U. S. Bankruptcy Law of July 1, 1898, § 57 (*h*).

[3] Ibid. (*a*); see The Skylark, 4 Biss. (U. S. Dis. Ct.) 388 (1869); Wicks *v.* Perkins, 1 Woods (U. S. Dis. Ct.), 383 (1871).

England nor in this country is the creditor bound to apply the security in diminution of his claim, nor to surrender it, unless the debt and the security rest upon the same estate. Our statute defines a "secured creditor" as one "who has security for his debt upon the property of the bankrupt, of a nature to be assignable under this Act, or who owns such a debt for which some indorser, surety, or other person secondarily liable for the bankrupt has such security upon the bankrupt's assets."[1]

Accordingly, if a firm creditor holds security upon the separate estate of a partner, he may prove his whole claim against the firm estate, nevertheless, and receive a dividend thereon, without having the security valued or sold.[2] For this purpose, the firm is treated both in England and in this country, as distinct from the individuals composing it, and the debts of the firm are sharply distinguished from the debts of the individual partners.

This topic will be referred to again in the section dealing with the order of proofs and marshalling.

### § 4. The Bankruptcy of the Firm.

When all the members of a firm are adjudicated bankrupts, it becomes the duty of the trustee to keep separate accounts of the partnership property and of the individual property of the partners.[3] Ordinarily the separation of the two estates is not a matter of difficulty. If, however, they have become inextricably blended, they may be consolidated;[4] but the mere fact that it is difficult to determine what is firm estate and what is separate property, or whether particular creditors are entitled to prove against

[1] U. S. Bankruptcy Law of July 1, 1898, § 1 (23).

[2] In re Thomas & Singer, 8 Biss. 139; 17 N. B. R. 54; 23 Fed. Cas. No. 13,886 (1878); Miller's River Nat. Bank *v.* Jefferson, 138 Mass. 111 (1884); Burdick's Cases on Part. 471.

[3] U. S. Bankruptcy Act of July 1, 1898, ch. 3, § 5 (*d*).

[4] Ex parte Sheppard, In re Bulwer, Mon. & Bl. 415 (1833).

the joint estate or the separate estates, will not justify the court in making a consolidation.[1]

1. Holding Out Partners. — In case persons are adjudicated bankrupts, who have held themselves out as partners, but between whom in fact there has been no partnership relation,[2] the question arises whether the assets of the apparent firm are to be treated as partnership property, or as the separate estate of their real owner.

In Great Britain, the answer is given by statute. A provision of the Bankruptcy Act[3] declares the property of a bankrupt divisible among his creditors shall include "all goods being, at the commencement of the bankruptcy, in the possession, order, or disposition of the bankrupt, in his trade or business, by the consent and permission of the owner thereof; provided that things in action other than debts due or growing due to the bankrupt, in the course of his trade or business, shall not be deemed goods within the meaning of this section."

The English courts have declared that the doctrine of reputed ownership, established by this statutory provision, does not apply to a case "where property belongs to a partnership of two, and there is only one ostensible partner. . . . The property is that of the two, and you cannot say that, because there is only one ostensible partner, the court will, in the event of bankruptcy, treat the property of the firm as in his order and disposition. The posses-

1 Ex parte Trotman, In re Kriegel, 5 Rep. (1893).

2 In Hanson *v.* Paige, 3 Gray (69 Mass.), 239 (1855), it was held that a mere partner by estoppel could not be adjudicated an insolvent in proceedings instituted by the actual partners; but in Re Kreuger, 2 Low. (U. S. Dis. Ct.) 66 (1871), it was decided that he could be adjudicated a bankrupt upon a petition of firm creditors. The U. S. Bankruptcy Law of July 1, 1898, § 5, does not seem to authorize an adjudication in bankruptcy of partners by estoppel, as a partnership. The adjudication would be against them as individuals.

3 Bankruptcy Act, 1883, § 44 (3).

sion in such a case is quite consistent with the real title, and therefore the reputed ownership clause does not apply." But when the real owner of property pretends to have formed a partnership with others, and permits this ostensible partnership to have possession and to appear as the owner of the property, the clause of the statute does apply, for the possession and apparent title are quite at variance with the real title.[1]

(*a*) *Various Views in this Country.* — We saw, in an earlier chapter, that some of our courts are disposed to expand this statutory doctrine of reputed ownership into a comprehensive principle of equity jurisprudence, and to hold, "that, if a person allows another to carry on business in such a way as to amount to a holding out to persons generally[2] that he and such other are partners, and a credit is given to both on the supposition that they are partners in fact, the property with which such business is carried on, though in law that of such person, in equity will be treated as the joint property of such person and such other; and neither of them, nor the creditors of either, can prove up in insolvency in competition with the creditors who have trusted the two as partners and the business as that of the two."[3]

[1] Ex parte Hayman, In re Pulsford, 8 Ch. D. 11, 22, 23 (1879), approving Reynolds *v.* Bowling, L. R. 1 Ch. 421 (1866), a case of a dormant partner. The doctrine of reputed ownership is fully treated in Lindley on Part. (6th ed.) Bk. 4 Ch. 4, § 3.

[2] In Ex parte Sheen, 6 Ch. D. 235 (1877), it was decided that the doctrine of reputed ownership did not apply where a person had been held out as a partner to some only of the creditors, there being no ostensible nor real partnership. Whitworth *v.* Patterson, 6 Lea (Tenn.), (1880) *accord.*

[3] *Supra*, Chap. II. § 4; Thayer *v.* Humphrey, 91 Wis. 276 (1895); Burdick's Cases on Part. 117, 121; Kelly *v.* Scott, 49 N. Y. 595 (1872), *accord.* Hillman *v.* Moore, 3 Tenn. Ch. 454, 458 (1877), approves of Kelly *v.* Scott, but refuses to apply the doctrine between execution creditors of the real owner and those of the ostensible firm.

This view has been repudiated in other jurisdictions, on the ground that while the person holding himself out as a partner is "under a personal estoppel to deny his liability, a creditor . . . cannot extend this estoppel so as to bind the property which was in the possession and use of the actual partners. The ostensible partner himself has no equity to have this property applied to the payment of the claims upon which he is liable, and therefore the creditors holding those claims who are merely subrogated to his rights and equities, have no such equity."[1]

A third view has been expressed by still other courts, viz., that the individual property which is used in such a a business is liable in the first instance for the individual debts of the owner; but that "the products of the business" are liable in the first instance for the business debts.[2]

2. THE CAPITAL OF A RETIRED PARTNER. — The doctrine of Thayer *v.* Humphrey[3] has been still further extended by the New York Court of Appeals, in a recent decision, which holds that "when a retired partner allows his unliquidated interest to be continued in the business of a new firm, the interest thus left becomes liable for the partnership debts subsequently incurred, as well as the prior debts," and that such retired partner cannot assume the position of a creditor of the new firm in competition with its other creditors, although the latter are notified of the dissolution of the old firm and become creditors of the new firm with such knowledge, and although the retired partner informed them that the capital which he had had in the business was, upon his withdrawal, loaned in part to his

[1] Broadway Nat. Bank *v.* Wood, 165 Mass. 312 (1896); Burdick's Cases on Part. 129, 130.

[2] Swann *v.* Sanborn, 4 Woods (U. S. Cir. Ct.), 625 (1878).

[3] 91 Wis. 276; Burdick's Cases on Part. 117, 121.

son, who succeeded him in the partnership, and the balance was loaned to the firm.[1] The only authorities cited in the prevailing opinion, for this conclusion, are quotations from Lindley[2] and from Parsons on Partnership. Both extracts are from passages dealing with the statutory doctrine of reputed ownership. The quotation from Parsons is followed by a note (not referred to by the court), to the effect that the cases "go no further than to hold that, where the real owner of the property stands by and virtually assents to its sale by the reputed owners, it is a fraud on the purchaser, and the real owner is estopped from subsequently setting up title."[3]

3. Conversion of Partnership Property into Separate Estate. — This subject was discussed quite fully in an earlier chapter,[4] and it will not be necessary at present to do more than recapitulate the conclusions then reached.

While a partnership is solvent it can by the agreement of all the partners convert the firm property into the individual property of the partners. If after such an agreement has been executed, the various partners become bankrupt, there will be no partnership estate for distribution.[5]

In case the agreement of partners is fraudulent as against the firm creditors, they or the trustee in bankruptcy may have the transfer set aside.[6] The same result may be attained in most jurisdictions, whenever

[1] Adams & Co. *v.* Albert, 155 N. Y. 356; 49 N. E. 929 (1898). The authority of this decision is weakened by the dissent of Vann, J., and Parker, C. J.

[2] Lindley on Part. 5th (ed.) 700, 702.

[3] Parsons on Part. (4th ed.) 492, note (*t*).

[4] *Supra*, Chap. III. § 3.

[5] Ex parte Ruffin, 6 Ves. 119 (1801); Burdick's Cases on Part. 192; In re Wiley, 4 Biss. (U. S. Dist. Ct.) 214 (1868).

[6] Wiggins *v.* Blackshear, 86 Tex. 670; 26 S. W. 939 (1894); Burdick's Cases on Part. 198.

the firm is insolvent at the time of the transfer,[1] or the agreement is made in contemplation of insolvency.[2]

In Peyser *v.* Myers,[3] the New York Court of Appeals declared: "The *corpus* of the firm property belongs to the firm, as an entity, and not to the individual partners. . . . This priority of lien of the firm creditors is not divested by a transfer by an insolvent firm of the firm assets to one or more of the partners, nor can it be affected, as we conceive, by any mere change in the personnel of the firm, as by the withdrawal of one partner from the firm on the introduction of a new member."

(*a*) *Agreement by Purchaser of Firm Title to Pay Firm Debts.* — It is well settled in England that the creditors of a firm do not become separate creditors of a partner by force of an agreement between the partners that one or more of them shall assume and pay the firm debts. "Unless the creditor accedes to that arrangement, he is not bound by it, nor can he avail himself of it; his position in fact is unaltered, he does not lose his old right, nor does he gain any new one."[4]

This doctrine has been adopted by a few of our courts; such an agreement being treated as "only a private executory contract, intended to regulate the rights, duties, and obligations of the copartners between themselves, consequent on a dissolution of the firm, to which the creditors were neither parties nor privies."[5]

Even when the consideration for this promise of the

[1] Jackson Bank *v.* Durfey, 72 Miss. 971; 13 So. 456 (1895); Burdick's Cases on Part. 201.

[2] In re Byrne, 1 N. B. R. 464 (1868); and see U. S. Bankruptcy Law of July 1, 1898, §§ 5, 67, and 70.

[3] 135 N. Y. 599, 604 (1892); 32 N. E. 699.

[4] Lindley on Part. (6th ed.) 723, note (*d*), and authorities there cited.

[5] Wild *v.* Dean, 3 Allen (85 Mass.), 579, 582 (1862).

partner who assumes the firm debts is the transfer to him of the firm title to its property, the firm creditors have no right, under the foregoing doctrine, to have such property distributed as partnership assets, unless the transfer can be set aside as fraudulent against firm creditors, or unless it appears that the retiring partners have retained their equitable right to have the firm property applied by the purchasing partner in discharge of firm debts.[1]

(*b*) *Prevailing View in this Country.* — Such is not the doctrine of the majority of our courts. On the contrary, the prevailing view[2] is that the firm creditors can avail themselves of the promise made by the purchasing partner to the retiring partner, as one made for their benefit: "That such promise, on the election of the creditors of the firm to avail themselves of it, is cumulative to their rights; that they need not release the firm in order to be able to obtain the benefit of such promise; and that such creditors may assent to and claim the benefit of such promise at any time, either before or after the bankruptcy of the promisor."

It is also held that the creditors of a sole trader can elect to avail themselves of an agreement, between him and his copartner, that the firm shall assume and pay his individual debts, provided the agreement does not operate as a fraud upon the other firm creditors.[3]

4. No Joint Estate and No Living Solvent Partner. — In case there is no partnership estate, and no living solvent partner, firm creditors are permitted to

[1] Ex parte Dear, 1 Ch. D. 514 (1876); In re Daniel, 3 Manson's Bky. R. 312; 75 L. T. 143 (1896); Howe *v.* Lawrence, 9 Cush. (Mass.) 553 (1852).

[2] In re Long and Corey, 7 Ben. (U. S. Dist. Ct.) 141, 148; 9 N. B. R. 227 (1874); In re Rice, 9 N. B. R. 373 (1874).

[3] Arnold *v.* Nichols, 64 N. Y. 117 (1876). In this case the agreement was made upon the formation of the partnership.

share *pari passu* with the individual creditors in the separate estates of the bankrupt partners.

This exception to the rule, which we have found to obtain in the distribution of firm and separate estates, has been much criticised,[1] but it has maintained itself both in England and in this country, even though its operations have been capricious, and although its existence has been ignored in the provisions of the bankruptcy statutes covering this topic. Such statutory provisions have been interpreted both in this country[2] and in England,[3] not as complete codifications which exclude reference to previous decisions or to previous legislation, but as legislative statements of the general principles which govern the distribution of property in bankruptcy proceedings. Accordingly, as the exception had been recognized and enforced by the courts, during a long period, it was not to be treated as abolished, in the absence of affirmative expressions to that effect.

A different view prevails in Massachusetts. The omission of this exception from the insolvency statute of that State has been held to indicate clearly the intention of the Legislature not to recognize its existence.[4]

(*a*) *Amount of Firm Estate.* — If any firm property comes to the hands of the trustee in bankruptcy for administration,[5] the firm creditors are precluded from sharing *pari passu* with the separate creditors in the individual estates of the partners. The amount is immaterial. "If, in point of fact, there is joint property, whether to the

[1] McCulloh *v.* Dashiell, 1 H. & Gill (Md.), 96, 105 (1827); Story on Part. (6th ed.) § 378; Pollock's Dig. of Part. (6th ed.) 149, 150.

[2] In re Knight, 8 N. B. R. 433; 2 Biss. (U. S. Cir. Ct.) 518 (1871).

[3] In re Budgett; Cooper *v.* Adams [1894], 2 Ch. 557.

[4] Howe *v.* Lawrence, 9 Cush. (Mass.) 553 (1852).

[5] Ex parte Hill, 2 B. & P. 191, note *a* (1802). In this case all the firm property was pledged to firm creditors for more than its value, and Lord Eldon held that it was a case of no joint effects.

amount of five pounds or five shillings," the firm creditors are confined in the first instance to such property.[1] The same result follows, in England, although the trustee is obliged to expend all of the joint funds in costs.[2]

In this country, however, it is held generally, that if the costs of the bankruptcy proceedings, or the expenses legally incurred in collecting firm assets, exhaust the firm estate, firm creditors may prove and share *pari passu* with separate creditors in the separate estates.[3] This conclusion was based in part upon the language of our bankruptcy statute.[4]

(*b*) *Odd Consequences of this Exception.* — Under the exception which we have been considering, it is quite possible for the separate creditors to benefit themselves by paying more than the market value for firm assets. If firm accounts are offered for sale, the separate creditors may pay a substantial sum for them, although they are deemed worthless, and thus put the partnership estate in funds and prevent firm creditors from sharing *pari passu* with the separate creditors in the separate estate.[5]

In the case last cited, the court viewed the exception as an arbitrary and inequitable one, and declared: "If we were to adopt the principle of going behind the fact of there being a fund, to inquire whether that had not been inequitably created by the management of the separate

1 Ex parte Peake, 2 Rose, 54 (1814).

2 Ex parte Kennedy, 2 De G. M. & G. 228 (1852).

3 In re McEwen & Sons, 12 N. B. R. 11 (1875); In re Slocum, 22 Fed. Cases, 338, Nos. 12,950, 12,951.

4 "The net proceeds of the partnership property shall be appropriated to the payments of the partnership debts, and the net proceeds of the individual estate of each partner to the payment of his individual debts." U. S. Bankruptcy Law of 1898, § 5 (*f*). The Act of 1867, ch. 176, § 36; U. S. R. S. § 5121, contained the words "net proceeds."

5 In re Marwick, 2 Ware, 229 (1845); Burdick's Cases on Part. 445, 447.

creditors, the court would at once be involved in inextricable difficulties."

(c) *No Living Solvent Partner.* — This term, in the exception now under consideration, means a non-bankrupt partner. Even though the partner who has not been adjudged a bankrupt is insolvent, yet as the firm creditors may proceed against him at law for the firm debts, their exceptional right in bankruptcy to share *pari passu* with separate creditors in the separate estate does not accrue.[1]

On the other hand, whenever a firm creditor cannot have an action at law and take out an execution against the representative of a deceased partner, his right to share with separate creditors in the separate estate of the bankrupt partner will not be affected by the fact that the deceased partner's estate is solvent.[2]

5. Exempt Property. — We have seen, in an earlier chapter,[3] that, according to the prevailing view, firm property is not included within the statutory exemptions from execution; that such exemptions are intended for the benefit of natural persons and are confined to the separate property of the partners.

The same doctrine is recognized by the weight of authority, in the case of exemptions under bankruptcy[4] or insolvency statutes. The right to exemption is an individual not a joint right; and the property which is exempted is individual, not joint property.[5]

[1] In re Marwick, in last note; Ex parte Janson, 3 Madd. 229 (1818).

[2] Ex parte Banerman, 3 Dea. 476, 486 (1838).

[3] *Supra,* Chap. III. § 2 (C).

[4] The present bankruptcy law of the United States exempts to bankrupts only such property as is exempt by the State statutes in their place of domicile at the time of filing the petition in bankruptcy, § 6.

[5] In re Corbett, 5 Sawyer (U. S. Dis. Ct.), 206 (1878); Ault-

### § 4. (A.) The Bankruptcy of a Partner.

When one or more, but not all, of the members of a firm are adjudged bankrupts, the trustees of such bankrupts do not become members of the partnership. To give them that position would be to violate that fundamental principal of partnership law which secures to each partner the right to choose his associates. Hence, the courts have uniformly held that upon the bankruptcy of a partner, his trustee cannot meddle with the interest of his copartners;[1] and that the trustee acquires title only to the individual property of the bankrupt and to his share or interest in the firm estate.[2] This share, as has been stated repeatedly, is the balance remaining after the payment of firm debts and the adjustment of the equities between the bankrupt and his copartners.[3]

1. THE TRUSTEE AND SOLVENT PARTNERS AS TENANTS IN COMMON. — The relation subsisting between the solvent partners and the trustee of a bankrupt partner is generally described as that of tenants in common.[4] If they are true tenants in common, it follows necessarily that neither has a legal right to call the firm property out of the hands of the other; and there is most respectable judicial authority in support of this conclusion.

Judge Lowell declared:[5] The trustee in bankruptcy "is tenant in common with the solvent partner of the joint stock. It usually happens that the latter will be in possession of the stock, and his possession will not be disturbed excepting for good reasons; and, on the other

man *v.* Wilson, 55 Ohio St. 138; 44 N. E. 1072 (1896); Burdick's Cases on Part. 448.

[1] Anonymous, 3 Salk. 61 (1696).

[2] Anonymous, 12 Mod. 446 (1701).

[3] Parker *v.* Muggridge, 2 Story (U. S. Cir. Ct.), 334 (1842).

[4] Lindley on Part. (6th ed.) 666.

[5] Wilkins *v.* Davis, 15 N. B. R. 60, 64 (1876).

hand, if, as in this case the assignee (trustee under the present statute) is in possession, that will not be disturbed without good cause."

Chancellor Kent went even further, declaring that the trustees of a bankrupt partner hold firm funds, of which they happen to gain possession, "by an equal title in law with him (the solvent partner), as tenants in common, and by a superior equitable title, as trustees, charged with the payment of both the joint and separate debts."[1]

(*a*) *The Modern Doctrine.* — Other judges, however, have entertained a different view.[2] Starting with the idea that a partnership is an entity distinct from the individuals composing it, whose title to firm property is not the sum of the several titles of its members, but is a peculiar species of ownership, these judges have declared that the bankruptcy of a partner does not "transfer the *corpus* of the partnership property"; that the dissolution of the firm, by the bankruptcy of a partner, does not devest the firm title; this remains intact, as it does upon dissolution by the natural death of a partner; and that the solvent partners have the same right to wind up the affairs of the firm as the surviving partner possesses.

The doctrine has received legislative approval in the United States Bankruptcy Law of 1898. It provides that: "In the event of one or more but not all of the members of a partnership being adjudged bankrupt, the partnership property shall not be administered in bankruptcy, unless by consent of the partner or partners not adjudged bankrupt; but such partner or partners not adjudged bankrupt shall settle the partnership business as expeditiously

[1] Murray *v.* Murray, 5 Johns. Ch. 60 (1821); Burdick's Cases on Part. 451.

[2] Jones *v.* Newsom, 7 Biss. (U. S. Cir. Ct.) 321 (1876); Ogden *v.* Arnot, 29 Hun (N. Y.), 146 (1883); Burdick's Cases on Part. 460, 461; *cf.* Collins *v.* Baker [1893], 1 Ch. 578.

as its nature will permit, and account for the interest of the partner or partners adjudged bankrupt."[1]

2. Transfers of Firm Property before Bankruptcy. — Where this doctrine prevails, a transfer by the firm of property in payment of a firm debt, although voidable under the statute by a trustee in bankruptcy of the firm, because made within a specified period before the filing of the petition in bankruptcy,[2] cannot be avoided by the trustee of a partner. Certainly such a preference is no fraud, either actual or statutory, upon the individual creditors of the bankrupt; and if the firm creditors would have it set aside as a preference in violation of the statute, they must take care that the partnership is adjudged a bankrupt within the time limited by statute.[3]

3. Liens on Firm Property before Bankruptcy. — Whether the bankruptcy of a partner will dissolve the lien of a levy under an execution or attachment which had been acquired by a firm creditor, depends upon the legal relation between the solvent partner and the bankrupt's trustee. If they are true tenants in common, and the trustee's title vests as of the date of the act of bankruptcy, the lien will be dissolved.[4]

On the other hand, if the firm title is unaffected by the bankruptcy of a partner, such bankruptcy will not impair the lien of an execution or attachment levied on behalf of firm creditors.[5] The latter view seems to have been embodied in the present bankruptcy statute of the United

[1] § 5 (*h*).

[2] U. S. Bankruptcy Law of July 1, 1898, §§ 67, 70.

[3] Forsaith *v.* Merritt, 1 Lowell (U. S. Dist. Ct.), 336 (1869); Burdick's Cases on Part. 458.

[4] Dutton *v.* Morrison, 17 Ves. 193 (1810); In re Wait, 1 Jac. & W. 605 (1820).

[5] Fern *v.* Cushing, 4 Cush. (Mass.) 357 (1849); Burdick's Cases on Part. 464; Mason *v.* Worthens, 7 W. Va. 532; 14 N. B. R. 346 (1874); Russell *v.* Cole, 167 Mass. 6 (1896); Burdick's Cases on Part. 469.

States.[1] Such a lien would not work a preference, for the firm creditors have the right to apply the firm estate to the payment of their debts, before the bankrupt's assignee can take anything. Moreover the statute provides that the property affected by the lien shall, after it is annulled, "pass to the trustee as a part of the estate of the bankrupt," thus showing that the liens referred to are those on the separate estate of the bankrupt.

4. Suits on Firm Claims or Liabilities. — Under the early English doctrine, that the solvent partner and the trustees of the bankrupt partner were tenants in common, it was held that they must join in actions at law for the enforcement of firm rights.[2] Such is still the rule in this country,[3] unless the provision of the Bankruptcy Law of 1898, securing to the non-bankrupt partners the right to settle the partnership business, has modified it. In the absence of statutory provision to the contrary, suits for the enforcement of partnership liabilities may be brought against all of the partners, although one or more are bankrupt, unless the latter have obtained their discharge in bankruptcy.[4]

In England, both of these rules have been changed by explicit provisions of the bankruptcy statute,[5] the most important of which is the following: "Where a bankrupt is a contractor in respect of any contract jointly with any person or persons, such person or persons may sue or be sued in respect of the contract without the joinder of the bankrupt." The present bankruptcy statute of the United

[1] Bankruptcy Law of 1898, § 67 (*c*), (*f*).

[2] Eckhardt *v.* Wilson, 8 D. & E. 140; 4 R. R. 618 (1799).

[3] Halsey *v.* Norton, 45 Miss. 703; 7 Am. R. 745 (1871); Browning *v.* Marvin, 22 Hun (N. Y.), 547 (1880); Russell *v.* Cole, 167 Mass. 6; 44 N. E. 1057 (1896); Burdick's Cases on Part. 469.

[4] Collyer on Part. (Wood's ed.) § 726; Parsons on Part. (4th ed.) § 375 and cases cited.

[5] Bankruptcy Act of 1883, §§ 10, 113, 114.

States contains no such provisions. It does not even give to the courts power to stay actions brought against the bankrupt after the filing of a petition against him.[1]

5. Discharge of a Bankrupt Partner. — The English statute makes it perfectly clear that the discharge of a bankrupt partner has the same effect, when the proceedings are against him individually, as when they are against the firm of which he is a member. In either case, he is freed from firm debts as well as from his individual debts, because every particle of his property — not only his separate property but his interest in the firm estate — is taken from him for the benefit of all his creditors.[2]

Whether the discharge of a partner, in bankruptcy proceedings against him individually, operated to free him from firm debts, was a subject upon which the decisions were at variance under former bankruptcy and insolvency statutes.[3] The present bankruptcy law of the United States appears to leave no ground for doubt on the subject. It takes from the bankrupt his share in the firm property as well as his individual estate; it permits firm creditors to prove against his estate; it provides that the liability of a co-debtor with the bankrupt shall not be altered by the bankrupt's discharge; and it declares that "a discharge in bankruptcy shall release a bankrupt from all his provable debts, except such as (1) are due as a tax levied by the United States, the State, county, district, or munic-

[1] U. S. Bankruptcy Act of 1898, § 11; *cf.* U. S. R. S. §§ 5105, 5106, for provisions of the Act of 1867 prohibiting suits against bankrupts, and providing for the staying of proceedings.

[2] Ex parte Hammond, L. R. 19 Eq. 614 (1873); Bankruptcy Act of 1883, § 30. The remarks in the text are made subject to the statutory exceptions, such as debts due the government, etc.

[3] Corey *v.* Perry, 67 Me. 140 (1877); Burdick's Cases on Part. 466, holds that his discharge does not extend to partnership debts. Mattix *v.* Leach, 16 Ind. App. 112; 43 N. E. 969 (1896); Burdick's Cases on Part. 468, holds that it does extend to firm debts.

ipality in which he resides; (2) on judgments in actions for frauds, or obtaining property by false pretences or false representations, or for wilful and malicious injuries to the person or property of another; (3) have not been duly scheduled in time for proof and allowance, with the name of the creditor, if known to the bankrupt, unless such creditor had notice or knowledge of the proceedings in bankruptcy;[1] or (4) were created by his fraud, embezzlement, misappropriation, or defalcation, while acting as an officer or in any fiduciary capacity."[2]

6. An Insolvent Firm of Solvent Partners.—In a jurisdiction where a partnership is treated as an entity, the firm may be proceeded against as an insolvent person, although one or more of its members may be able to pay his or their individual debts as well as the firm debts in full. "Although the partners as individuals may be perfectly solvent, the firm, as such, may be insolvent."[3]

Under our present bankruptcy law, it appears to be possible to have a partnership adjudicated a bankrupt, while the partners remain solvent. This statute declares that "a partnership . . . may be adjudged a bankrupt;" that a person who suffers or permits, "while insolvent, any creditor to obtain a preference through legal proceedings, and not having at least five days before a sale or final disposition of any property affected by such preference, vacated or discharged such preference," commits an act of bankruptcy; that the words "'persons' shall include . . . partnerships"; that "it shall be a complete defence to any proceedings in bankruptcy . . . to allege and prove that

[1] Had this provision appeared in the Bankruptcy Act of 1867, probably it would have warranted the conclusion reached in Corey *v.* Perry, *supra.*

[2] U. S. Bankruptcy Law of 1898, §§ 5 (*h*), 63, 16, and 17.

[3] Ransom *v.* Woodlaw Co. 99 Ga. 540 (1896); Burdick's Cases on Part. 468, *n.*

the party proceeded against was not insolvent as defined in this Act at the time of filing the petition against him, and if solvency at such date is proved by the alleged bankrupt, the proceedings shall be dismissed"; and that a person is deemed insolvent, "whenever the aggregate of his property, exclusive of any property which he may have conveyed, transferred, concealed or removed, or permitted to be concealed or removed, with intent to defraud, hinder or delay his creditors, shall not at a fair valuation be sufficient in amount to pay his debts."[1]

In Massachusetts, however, it is held that a court of insolvency acquires jurisdiction to settle the affairs of a partnership, under the insolvency law of that State "only when two or more persons who are partners become insolvent, that is, when the partnership is insolvent through the insolvency of all the members of the firm."[2]

§ 4. (B.) **Order of Proofs and Marshalling.**

When a court of bankruptcy or insolvency is administering the firm estate as well as the separate estates of the partners, important and sometimes difficult questions arise concerning the order in which claimants are to share the estates, and the manner in which the different funds are to be marshalled.

1. Creditors holding Joint and Several Obligations. — If a creditor has obtained the obligation of the firm and the several obligations of the partners for the same debt, he ought to "have the benefit of the caution he has used," and, upon the bankruptcy of the partners, to be permitted to prove against both the firm and the separate estates.[3] The English bankruptcy courts reached a

[1] U. S. Bankruptcy Law of 1898, §§ 5 (*a*), 3 (*a*), (*c*), 1 (*a*), (15), (19).

[2] Russell *v.* Cole, 167 Mass. 6; 44 N. E. 1057 (1896); Burdick's on Part. 469, construing § 120, Ch. 157, Genl. Laws.

[3] Lord Eldon, in Ex parte Bevan, 10 Ves. 107 (104).

different conclusion, however, and, in the case last cited, Lord Eldon was forced to admit that it was settled, that "the advantage of a joint and separate creditor is no more than that he can elect whether he will be in the first instance a joint or a separate creditor; but if he has once elected, his fate must be the same as that of all other joint creditors."

The reasons assigned by the English courts for adopting this rule were the following, in brief: That the obligors in a joint and several bond cannot be sued at one and the same time both jointly and severally, but the obligee must make his election; hence, the obligee should not be allowed to prove in bankruptcy against both estates at once.[1] That, although at law, if the obligee sued the obligors jointly, he might levy his execution upon both the joint and the several property of the partners, yet to permit the obligee to take dividends on the same debt from both estates in bankruptcy would be to give him a preference over other joint creditors in the firm estate, and a preference over the other separate creditors in the separate estate, which, it was thought, would violate the fundamental principle of bankruptcy law, "that all persons should have an equal satisfaction, and not one more than another."[2]

(*a*) *The Present Rule.* — In England, the foregoing rule has been so modified by statute as to permit a creditor, holding a joint and several obligation, to prove against both estates, providing that the joint and the separate liabilities arise out of "distinct contracts."[3] While the

[1] Ex parte Rowlandson, 3 P. W. 405 (1735).

[2] Ex parte Bond and Hill, 1 Atk. 98 (1743). These cases also settled the law, that the creditor was entitled to a reasonable time to inquire into the state of the funds, before making a final election.

[3] Bankruptcy Act of 1883, Sched. 2, § 18, re-enacting § 37 of Act of 1869; *cf.* Ex parte Honey, L. R. 7 Ch. 178 (1871), a joint and several

statute does not abrogate the old rule entirely, yet as "joint and several liabilities arising otherwise than by distinct contracts are, comparatively speaking, few in number," the remnant of the old rule is "practically of little consequence to partners or their creditors."[1]

The earlier English rule never found favor in this country, and has been expressly repudiated by Federal and State courts.[2] In a leading case upon this topic, the learned judge declared: "In this country . . . existing contracts have been made under, and with reference to the rule of law which gives to a party holding two valid obligations the benefit of both. This right, founded both in law and justice, I do not think myself bound or authorized to set aside on account of an arbitrary rule, justly reprobated by the most eminent judges and jurists in England, and never recognized in this country."[3] While the United States Bankruptcy Law of 1898 does not expressly grant the right of double proof to a creditor holding the joint and several obligations of partners, it contains no provision denying this right. On the other hand, many of its provisions bearing on this subject are similar to those contained in the Act of 1867; and that Act was construed as sanctioning the right of double proof.

(*b*) *A Peculiar Doctrine in Kentucky.* — On a previous page[4] the fact has been noted, that the equity rule in Kentucky for distributing the partnership and the separate estates to the two classes of creditors is a peculiar one. That

note; Ex parte Stone, L. R. 8 Ch. 914 (1873), joint and several bond.

[1] Lindley on Part. (6th ed.) 766.

[2] Emery *v.* The Canal Nat. Bank, 3 Cliff. (U. S. Cir. Ct.) 507, 7 N. B. R. 217; 5 L. T. B. 419 (1872); Ex parte Mason, 70 Me. 363 (1880); Roger Williams Nat. Bank *v.* Hall, 160 Mass. 171 (1893); Burdick's Cases on Part. 473.

[3] In re Farnum, 6 Bos. L. R. 21 (1843).

[4] *Supra*, 272 *n.* 8.

rule is applied even against a creditor who has secured the joint and several obligations of the partners. He is not allowed to reap the benefit of his diligence. He must elect to proceed in the first instance either against the firm estate or the several estates. Having so elected, and taken his dividend from the chosen estate, he cannot share in the other estate until the other creditors of such estate have received a dividend equal to that which has been paid to him.[1]

2. A PARTNER AS CREDITOR OF THE FIRM. — "In keeping partnership accounts the firm is made debtor to each partner for what he brings into the common stock."[2] The English common law, as we have seen, does not adopt this view of the relations subsisting between a firm and its members. It is true that Lord Hardwicke treated a bankrupt firm and its members as distinct persons, and allowed the individual estate of a creditor partner to prove against the firm estate, and the firm to prove against a debtor partner.[3] That practice was changed by his successor, and for more than a century the rule which has prevailed in bankruptcy cases in England has been, that a partner "shall not prove in competition with the creditors of the firm." The reason assigned for the rule is that such creditors being "in fact his own creditors," he "shall not take part of the fund to the prejudice of those who are not only creditors of the partnership but of himself."[4]

(a) *Rule of United States Bankruptcy Law of* 1898. — This statute appears to have restored Lord Hardwicke's

[1] Hill *v.* Cornwall, 95 Ky. 512; 26 S. W. 540 (1894); Burdick's Cases on Part. 474.

[2] Bank of Buffalo *v.* Thompson, 121 N. Y. 280 (1890); Burdick's Cases on Part. 286, 288, quoting Lindley on Part. (5th ed.) 110.

[3] Lord Blackburn in Read *v.* Bailey, 3 App. Cas. 94, 101 (1877), referring to Ex parte Hunter, 1 Atk. 357 (1742).

[4] Ex parte Sillitoe, 1 Gl. & J. 374 (1824); Gibbs *v.* Humphrey, 91 Wis. 111; 64 N. W. 750 (1895); Burdick's Cases on Part. 475.

practice, and to "permit the proof of the claim of the partnership estate against the individual estates, and *vice versa*."[1] It is difficult to give to the language just quoted any other construction, especially if we keep in mind the conception of a partnership as "a person," which finds repeated expression in this statute; and yet, if this is the proper construction of that clause, it must be admitted that this brief provision works a radical and important change in this branch of the law.

(*b*) *Exceptions to the Old Rule.—First.* After stating the English rule, in the language which has been quoted from Ex parte Sillitoe,[2] Lord Eldon said: "To that rule there is an exception, manifestly founded in justice, and that is, when a partner becomes a creditor in respect of the fraudulent conversion of his separate estate to the use of the partnership, an exception established in Ex parte Kendal[3] and other cases."

The question, what amounts to a fraudulent conversion of a partner's property by the firm, so as to give to the estate of the defrauded partner this exceptional right to prove against the firm estate, has not been an easy one for the courts. Lord Eldon intimated that the fraud must be such as would warrant the representation that it had been stolen.[4] Certainly the misconduct must be something more than a breach of the duty which each partner owes to his copartners, of exercising the utmost good faith in partnership dealings; more even than a deliberate violation of the

[1] § 5 (*g*), *cf.* § 56 (*m*), also § 5 (*a*), § 3 (*d*), and § 1 (19).

[2] 1 Gl. & J. 374 (1824).

[3] 1 Rose, 71. This reference is certainly erroneous. Probably Lord Eldon referred to Ex parte Lodge and Fendal, 1 Ves. Jr. 166 (1790). See his reference to this as the leading case in point, in Ex parte Harris, 1 Rose, 437, 438.

[4] Ex parte Yonge, 3 Ves. & B. 31 (1814), adopted in Lindley on Part. (6th ed.) 752.

partnership articles;[1] it must amount, at least, to a fraudulent conversion of the separate property of the partner to the use of the firm, without such partner's consent or subsequent ratification.[2] But it seems to be settled that it need not amount to more than this.

Accordingly, if the partner's property is used for the firm without his knowledge or consent, and if that use is concealed from him by means of fictitious entries in the partnership books, his estate may prove therefor against the firm estate.[3]

(c) *Second Exception — Trade Debts.* — Another exception has long been recognized in England, under which the estate of one or more members of a firm may prove against the firm estate for a trade debt. In order to bring a case within this exception, it must appear that the creditor partner or partners were carrying on a business wholly distinct from that of the firm, and that the debt was contracted for articles furnished to the firm by the creditor partner or partners in the ordinary course of dealings between the two trades.[4] If all that can be shown is that the creditor estate has loaned money to the firm, the general rule applies, and cuts the estate off from the benefit of proof.[5]

This exception was favored by Lord Eldon because of the complicated nature of modern commercial relations which had compelled the courts to "say that a man may

[1] Blackburn, L., in Read *v.* Bailey, 3 App. Cas. 94, 103 (1877), explaining Lodge and Fendal, 1 Ves. Jr. 166.

[2] Pollock's Dig. of Part. (6th ed.) 154.

[3] Haines & Co.'s Estate; Grove's Appeal, 176 Pa. St. 354; 35 At. 237 (1896); Burdick's Cases on Part. 482.

[4] Ex parte Sillitoe, 1 Gl. & J. 374 (1824).

[5] Ex parte Hargreaves, 1 Cox, 440; 1 R. R. 74 (1788); Rogers *v.* Meranda, 7 Ohio St. 179 (1857); Burdick's Cases on Part. 424, 432; Gibbs *v.* Humphrey, 91 Wis. 111; 64 N. W. 750 (1895); Burdick's Cases on Part. 475.

be half a dozen men for the purpose of binding himself and benefiting others, and for that purpose may put his name upon bills in different characters, and may be a member of many partnership houses." [1] Lord Brougham supported the exception on the ground that the dealers who supplied the business of the creditor partner with goods which were sold by him to the firm might fairly be considered as creditors of such firm, "inasmuch as the" creditor partner's "house was no more than a sort of funnel for the transmission of the goods; and there would seem no injustice, therefore, in allowing them to go at once *per saltum* and prove against the parties to whom the goods were really supplied." [2]

(*d*) *Exception Limited in this Country.* — Our courts have refused to accept Lord Brougham's view. They permit one firm to prove against another, provided all of the members of the proving firm are not included in the other; [3] but they refuse to allow proof by the estate of a partner, or of a firm all of whose members are partners in the debtor firm, although the claim has arisen between distinct trades.[4] The reason given for this holding is, that, as the partner or the smaller firm could not, if solvent, "claim anything against the copartnership assets until its creditors, who are also his creditors, are fully paid, his creditors upon his insolvency can take no greater rights than he had."

(*e*) *Third Exception: Proof by a Discharged Partner.* — As the rule which prohibits a partner from proving against the firm estate is founded upon the principle that

[1] Ex parte Sillitoe, 1 Gl. & J. 374 (1824).

[2] Ex parte Cook, Mon. 228 (1831).

[3] In re Buckhouse, 10 N. B. R. 206; 2 Low. (U. S.) 331 (1874).

[4] In re Savage, 16 N. B. R. 368, 370 (1877). In re Rieser, 19 Hun 202 (1879), affirmed on the opinion of the court below, 81 N. Y. 629 (1880). In re Lane, 10 N. B. R. 135; 2 Low. (U. S.) 333 (1874).

he ought not to be a competitor with his own creditors, as soon as he ceases to be liable to firm creditors, the reason for the rule ceases. Hence, a partner who has been discharged in bankruptcy, or otherwise, from firm debts, is allowed to prove any valid claim which he thereafter holds against the firm estate.[1] The same result follows, when the claims of partnership creditors have become barred by the statute of limitations as against the creditor partner's estate.[2]

(*f*) *Proof by Purchaser of Creditor Partner's Claim.* — In case the creditor partner transfers his claim against the firm to a *bona fide* purchaser prior to the institution of bankruptcy proceedings, the transferee can prove it against the firm estate and share with other firm creditors;[3] but if the transferee is not a *bona fide* purchaser, he can "occupy no higher ground in the distribution than" his transferrer "would have occupied," and his proof will be postponed to the claims of the firm creditors.[4]

(*g*) *A Partner as a Surety for the Firm.* — It sometimes happens that a firm creditor receives individual property of a partner as collateral security. If he sells this and applies the proceeds to the satisfaction of the firm debt, the partner is entitled to reimbursement from the firm. But if the partner has not been reimbursed before bankruptcy proceedings are commenced, the general rule which we have been considering prohibits his estate from proving this claim against the firm estate. In case the creditor applies the security to the payment of the

1 Ex parte Atkins, 1 Buck, 479 (1820).

2 In re Hepburn, Ex parte Smith, 14 Q. B. D. 394 (1884).

3 Miller's River Nat. Bank *v.* Jefferson, 138 Mass. 111 (1884); Burdick's Cases on Part. 471.

4 McCruden *v.* Jonas, Yetta Greenboum's Appeal, 173 Pa. St. 507; 34 At. 224 (1896); Burdick's Cases on Part. 478.

debt after bankruptcy, however, the separate estate is not without remedy. It cannot make formal proof against the firm estate, it is true, for to permit that would be to violate the bankruptcy rule of distribution; but a bankruptcy court, in the exercise of its equity powers, will order the separate estate to be reimbursed to the amount which such a proof would have produced.

In support of this practice, it is said, the joint creditors could not have been heard to complain if the second creditor had seen fit to surrender the collaterals, and to prove his debt against the partnership estate. As he did not see fit to exercise this option, but satisfied his claim out of the separate property of the partner, the separate creditors of that partner should be subrogated to the rights of the secured firm creditor against the firm estate.[1]

By the present bankruptcy statute of the United States, "the technical difficulties in the way of obtaining relief" by a proof of the creditor partner's claim against the partnership estate appear to have been removed, and resort to "the benign vigor of the rules of equity" is no longer necessary in order to evade the general bankruptcy rule of distribution. The separate estate may now accomplish directly, whenever it is a creditor of the firm estate, what could be gained formerly in but a limited class of cases and then only by indirection and through equitable circumlocution.

3. The Firm as a Creditor of a Partner. — Our Federal bankruptcy statute also recognizes the right of the firm estate to prove against the individual estates of the partners.[2] This is not permitted in England, nor has it been allowed under other statutes in this country, except in a few cases soon to be mentioned. As English law does not recognize a firm as an entity, but as an association of

[1] In re Foot, 12 N. B. R. 337 (1875); Burdick's Cases on Part. 480.
[2] U. S. Bankruptcy Law of 1898, § 5 (*g*).

individuals, to say that a partnership may prove against its members is to say that a man may prove with others against himself.[1]

(*a*) *First Exception: Fraudulent Conversion by a Partner.* — This is but the converse of an exception, which we have found to exist in favor of proof by a partner. Perhaps, the best statement of the principle upon which it rests is found in the following extract from an opinion of Lord Chancellor Cairns:[2] "So long as you have distinct estates, so long as you keep distinct the joint estate and the separate estate, if you allow the firm, the partnership concern, to make contracts with its separate members, and to stand upon those contracts as affording a ground of proof as against the separate creditors, you run a risk, to say the least — perhaps I might say you have the certainty — that contracts will be made between the firm and the individual members which in effect will defeat the rights of the creditors of the individual members. But where you have a conversion of the property of the firm to the purposes of the individual members, not by way of contract or agreement with the firm, not within the knowledge or the cognizance of the firm, but by a fraud of an individual partner, to which the firm is no assenting party, of which its other members are not cognizant and cannot be cognizant, there the reason for the rule ceases, and the firm whose assets have thus been fraudulently abstracted ought not to suffer, and ought not to be deprived of the right to proceed against the separate estate in competition with any other claimants. Whether the separate estate has in the result been increased or not, — whether at the time of the proof it is larger than it otherwise would have been or not, — is a matter which does not concern the application of the rule,

[1] Lindley on Part. (6th ed.), 756.

[2] Read *v.* Bailey, 3 App. Cas. 94 (1877).

and it is sufficient that at one time the separate estate was increased when the property was thus fraudulently converted and taken for the purpose of one partner."

(*b*) *Second Exception: Trade Debts.* — This exception, like the corresponding exception in favor of a creditor partner, is based upon the mercantile view of the relation subsisting between a partnership and its members. According to that view, the partnership may be a creditor of a partner, and a partner may be a creditor of the partnership. In establishing the present exception, English judges have acted in a characteristic manner. They have adopted mercantile usage in part, and have rejected it in part. Only when the firm becomes a creditor of a partner, or of a distinct firm composed of some of its members, as the result of business dealings between the principal firm and the partner or smaller firm carrying on a distinct trade, is the trustee of the principal firm estate allowed to prove against the estate of the partner or of the smaller firm.[1]

This exception has not been recognized by the courts in this country.[2]

4. A Partner as a Creditor of a Copartner. — Neither a solvent partner nor the estate of a bankrupt partner is allowed to prove against a copartner's estate in competition with the firm creditors. This is entirely in accordance with the principle underlying the general rule which we have been considering. If he has paid all the partnership debts,[3] or if they have been barred by the statute of limitations, or in any other way have ceased to

[1] Ex parte St. Barbe, 11 Ves. 413 (1805); Ex parte Castell, 2 Gl. & J. 124 (1826).

[2] Cases cited *supra*, p. 298, *n.*; McCruden *v.* Jonas, Burdick's Cases on Part. 478.

[3] In re Dell, 5 Sawyer (U. S. Dist. Ct.) 344 (1878). The mere fact that he has indemnified the joint estate will not entitle him to prove against the separate estate. Ex parte Moore, 2 Gl. & J. 166 (1826).

exist as against him,[1] he may prove against his debtor partner's estate. So he may if that estate is insufficient to pay the other separate creditors in full; for in that case there is no possibility of his claim competing with the claims of the joint creditors.[2]

As a creditor of his bankrupt copartner he has the same rights against the debtor's individual property as are possessed by other separate creditors, while with regard to the bankrupt's share in the firm property he may have an advantage over them. For example, if a balance is due to him from the firm, after the payment of firm creditors and the adjustment of partnership accounts, he has a lien therefor upon the bankrupt's share of the remaining partnership funds. All that the other separate creditors of the bankrupt can claim, as his share, is "that part of the partnership effects which shall remain after the demands of his partner upon the partnership are satisfied." If this share is insufficient to pay the balance due the creditor partner, he is entitled to prove for such deficiency *pari passu* with the other separate creditors of the bankrupt.[3]

(*a*) *Assignee of a Creditor Partner.* — A *bona fide* transferee of a creditor partner's claim against a copartner is entitled to prove against the debtor partner's estate, whether firm creditors have been paid or not. They are not his creditors, and therefore the principle which would have postponed proof by his assignor does not affect him. If the transferee is not a *bona fide* purchaser, he will be subject to the disabilities of his transferrer, unless he can show that he has been substituted by a valid novation as a creditor of the now bankrupt partner.[4]

But even in such a case, if the claim in the form of a

[1] Ex parte Grazebrook, 2 Dea. & Ch. 186 (1832),

[2] Ex parte Topping, In re Levey, 4 De G. J. & S. 551 (1865).

[3] Ex parte King, 17 Ves. 115 (1810).

[4] Ex parte Todd, De G. 87 (1844); Parsons *v.* Tillman, 95 Ind. 452 (1884).

negotiable note from the debtor partner to the assignor be transferred while the parners are solvent, and thus free from equities at that time, the transferee will not be affected by subsequent dealings and complications between the partners. On the other hand, he may prove his claim even in competition with joint creditors.[1]

5. Separate Estate of a Partner in an Illegal Partnership. — Even when the partnership is illegal, it is perfectly lawful for one of the partners to assign his interest in the firm property to his copartner, to be applied by the latter for the benefit of firm creditors. If the assigning partner thereafter becomes bankrupt, his separate creditors have no right to complain of the assignment. The property acquired by the illegal partnership was not the several property of the partners, simply because the partnership was illegal; nor had the "individual creditors of one of the partners a prior right to satisfaction out of such assets over the creditors of the partnership."[2]

### § 5. Death of a Partner.

The effect of a partner's death upon the title to firm property, and the liabilities of the surviving partners to firm creditors, have been dealt with in a former chapter. It is the purpose of the present section to state the rights and remedies of firm creditors against the deceased partner's estate.

1. The Rule in Great Britain. — This is stated in the Partnership Act[3] as follows: "Every partner in a firm is liable jointly with the other partners, and in Scotland severally also, for all debts and obligations of the firm incurred while he is a partner; and after his death his

[1] First Nat. Bank of Champlain v. Wood, 128 N. Y. 35; 27 N. E. 1020 (1891).

[2] Patty-Joiner Co. v. City Bank, 41 S. W. 173; 15 Tex. Civ. App. 475 (1897); Burdick's Cases on Part. 484.

[3] Partnership Act of 1890, § 9.

estate is also severally liable in a due course of administration for such debts and obligations, so far as they remain unsatisfied, but subject in England or Ireland to the prior payment of his separate debts."

Prior to the decision of Kendall v. Hamilton,[1] there was abundant authority in England for the statement that, "in the consideration of a court of equity, a partnership debt is several as well as joint."[2] The House of Lords decided, however, in Kendall v. Hamilton that this was an inaccurate statement; that the liability of partners for firm debts is joint in equity as well as in law; but that as in equity there is no survivorship of property, so there is in equity no survivorship of liability. It is true that, after the death of a partner, firm creditors can sue only the survivors at law; "but that is only because the executors of a deceased partner never could be sued at law."[3] The estate of the deceased partner remains liable to firm creditors in equity, and is entitled to receive from the survivors his share of the firm estate.

Nor does it matter, in England, "in what order the partnership creditor pursues his concurrent remedies, provided the two following conditions are substantially satisfied: first,[4] he must not compete with the deceased partner's separate creditors; secondly,[5] the surviving partner must be before the court."[6]

2. Conflicting Rules in this Country. — The English rule prevails in many of our States, where it is held that "Every partnership debt being joint and several, it

[1] 4 App. Cas. 504 (1879).

[2] Wilkinson v. Henderson, 1 M. & K. 582 (1833); Pollock's Dig. of Part. (5th ed.), 40.

[3] Mellish, L. J., in Beresford v. Browning, 1 Ch. D. 30 (1875).

[4] Gray v. Chiswell, 9 Ves. 118 (1802).

[5] Wilkinson v. Henderson, 1 M. & K. 582 (1833); In re Hodgson, Beckett, & Ramsdale, 31 Ch. D. 177 (1885).

[6] Pollock's Dig. of Part. (5th ed.), 40.

necessarily follows that resort may be had, in the first instance, for the debt, to the surviving partners, or to the assets of the deceased."[1]

On the other hand, the weight of authority in this country, in the absence of statutory provisions on the subject, favors the rule that upon the death of a partner, firm creditors cannot proceed in equity against his estate "without showing, either that the surviving partners have been proceeded against to execution at law, or that they are insolvent."[2] In Voorhis *v.* Child's Executor this rule is supported on the following grounds: "The surviving partners succeed primarily to all the rights and interests of the partnership. They have the entire control of the partnership property, and the sole right to collect the partnership dues. The assets of the firm are of course to be regarded as the primary fund for the payment of the partnership debts, and it would seem equitable, at least, that the parties having the exclusive possession of this fund should be first called upon. The answer given to this by the English courts, that the representatives of the deceased partner have their remedy over, seems hardly satisfactory. The presumption is, that the primary fund is sufficient to meet the demands upon it. Why, then, permit in equity a resort to another fund, and thus give rise to a second action for its reimbursement. Besides, these English decisions permitting the creditor to proceed in the first instance in equity against the estate of the deceased partner are in conflict with the established doctrine, that parties must first exhaust their legal remedies before resorting to courts of equity."

(*a*) *No Joint Estate or Living Solvent Partner.* — In some American jurisdictions firm creditors are not allowed

[1] Doggett *v.* Dill, 108 Ill. 560 (1884); Burdick's Cases on Part. 495, 496, and cases cited in the opinion.

[2] Voorhis *v.* Child's Executor, 17 N. Y. 354 (1858); Burdick's Cases on Part. 490, 491; Pope *v.* Cole, 55 N. Y. 124 (1873).

to compete with the separate creditors of a deceased partner, even though there is no joint estate and no living solvent partner.[1]

(b) *Statutory Provisions.* — In Rhode Island it is declared by statute that "unless otherwise provided in the contract, upon the death of any joint contractor, his representatives may be charged in the same manner as such representatives might have been charged if such contract had been several instead of joint: provided that the plaintiff shall first exhaust the partnership estate if such contract is a partnership contract."[2]

In a number of States the liability of partners for firm debts has been changed by legislation from joint to joint and several.[3] The language of the New York statute, referred to in the last note, is as follows: "Every general partner is liable to third persons for all the obligations of the partnership, jointly and severally with his general copartners." This appears to abrogate the rule laid down in Voorhis *v.* Child's Executors,[4] and to give to partnership creditors the right to proceed against a deceased partner's estate in the first instance, and to share *pari passu* with his separate creditors.[5]

[1] Stewart's Case, 4 Abb. Pr. (N. Y.) 408 (1857); Burdick's Cases on Part. 493; Warren *v.* Farmer, 100 Ind. 593 (1884).

The English courts recognize an exception in such cases; but if the separate creditors show that there was joint estate at one time available to firm creditors, this will bar the latter from competing with the former, although before the separate estate is brought into a court of equity for distribution, the joint estate has been exhausted. Lodge *v.* Prichard, 1 De G. J. & S. 610 (1863).

[2] Island Savings Bank *v.* Galvin, 19 R. I. 569; 36 At. 1125 (1896); Burdick's Cases on Part. 500.

[3] Stimson's Am. St. Law, § 4113; Ch. 420 Laws of N. Y., 1897, § 6.

[4] 17 N. Y. 354 (1858); Burdick's Cases on Part. 490.

[5] Matter of Gray, 111 N. Y. 404 (1888); 18 N. E. 719.

# CHAPTER VI.

## DUTIES AND LIABILITIES OF PARTNERS INTER SE.

### § 1. The Utmost Good Faith.

One of the cardinal obligations of a partner is to exercise perfect fairness and good faith towards his associates in all partnership matters. "If fiduciary relation means anything," said an eminent English judge, "I cannot conceive a stronger case of fiduciary relation than that which exists between partners. Their mutual confidence is the life blood of the concern. It is because they trust one another that they are partners in the first instance; it is because they continue to trust one another that the business goes on."[1] No stipulation on this subject is needed in the partnership articles. The duty to observe the utmost good faith is imposed upon the partners by the partnership relation.[2]

(a) *Preliminary Negotiations.* — Even in matters preliminary to the launching of the partnership, each member is subject to this duty. If the partnership is to be formed for the purpose of buying certain property with a view of selling it at a profit, a partner who secures title to it before the partnership is organized is bound to turn it over to the firm at the price which he paid.[3] In case one partner induces the other to enter into copartnership by means

[1] Bacon, V. C., in Helmore *v.* Smith, 35 Ch. D. 436, 444 (1887).

[2] *In societatis contractibus fides exuberet,* Cod. iv. 37, 3; Pollock's Dig. of Part. (6th ed.), 85.

[3] Hichens *v.* Congreve, 1 R. & M. 150 (1829); Bloom *v.* Lofgren, 64 Minn. 1; 65 N. W. 960 (1896); Burdick's Cases on Part. 501.

of fraudulent representations as to the property which the former puts into the business, the latter may have the partnership contract annulled, and may recover whatever he has contributed to the firm. It is not necessary for him to show that he has sustained actual damage. He is entitled to be released from partnership relations with one who has thus betrayed his confidence.[1]

(*b*) *Purchase of a Copartner's Interest.* — A partner, who seeks to acquire his copartner's interest in the firm, is bound to act with the utmost frankness and honesty. Not only must he render true accounts of all business transactions, but he must give "full information of all things affecting the partnership."[2] If he knows that his copartner is "laboring under incorrect views in reference to the amount of the debts due by the concern," or in reference to the fair value of its assets, it is "his duty to furnish all the data he may have, by which such views may be corrected."[3] Certainly, if he has entered into trade combinations whereby the value of the partnership business has been increased, it is his duty to inform his copartner of this fact. Suppression of this fact and a purchase upon the basis of the apparent valuation will amount to a fraud upon the ignorant copartner.[4]

(*c*) *Clandestine Profits.* — A partner who secures any private advantage or benefit from "any transaction concerning the partnership, or from any use by him of the partnership property, name, or business connection," without his copartners' consent, even though the transactions are "undertaken after a partnership has been dissolved by the death of a partner, and before the affairs thereof

[1] Harlow *v.* La Brum, 151 N. Y. 278; 45 N. E. 859 (1897); Burdick's cases on Part. 502.

[2] British Partnership Act (1890), § 28.

[3] Sexton *v.* Sexton, 9 Gratt. 204, 215 (1852).

[4] Meyers *v.* Merillion, 118 Cal. 352; 50 Pac. 662 (1897).

have been completely wound up,"[1] acts in bad faith towards his associates or their representatives, and can therefore be compelled to account for the profits which he has gained.

Accordingly, if a lease of premises occupied by the firm is secretly renewed by a partner in his name, the firm will be entitled to the lease. He will not be permitted to say to his copartner, "The premises on which we carried on our trade have become mine exclusively; and I am entitled to demand from you whatever terms I think fit, as the condition of permitting you to carry on that trade."[2] Again, in case a partnership exists for the purpose of locating and developing mining properties, all mines located and sold by any of the partners during the partnership must be accounted for to the firm.[3] So secret commissions received by a partner on firm purchases[4] or firm sales[5] belong to the firm.

(*d*) *Prohibited Competition.* — When a partnership has been formed with a view to reaping the profits of a particular business, none of its members can carry on a "business of the same nature as and competing with that of the firm," without cutting down its profits. Hence, if he does carry on such a business, without his copartners' consent, "he must account for and pay over to the firm all profits made by him in that business."[6]

(*e*) *Non-competitive Transactions.* — Although a partner carries on a business for his private benefit which is similar to that of the firm, he will not be answerable to his copartners for the profits if the business is really different

[1] British Partnership Act (1890), § 29.

[2] Featherstonaugh *v.* Fenwick, 17 Ves. 298; 11 R. R. 77 (1810).

[3] Jennings *v.* Rickard, 10 Col. 395; 15 Pac. 677 (1887).

[4] Hodge *v.* Twitchell, 33 Minn. 389; 23 N. W. 547 (1885).

[5] Newell *v.* Cochran, 41 Minn. 374; 43 N. W. 84 (1889).

[6] British Partnership Act, 1890, § 30; Latta *v.* Kilbourn, 150 U. S. 524, 541 (1893); Burdick's Cases on Part. 503, 508.

from that of the firm. For example, a member of a firm of warehousemen does not compete with his partnership in owning and managing wharf boats.[1] Nor does a partner in a firm of real estate brokers interfere with its business by engaging in the purchase and sale of real estate as an individual speculation.[2] The case last cited shows that the question of fact whether a partner is carrying on a business in competition with his firm may be a difficult one, — one upon which different courts will entertain contradictory opinions, but that the rule of law applicable, when the facts have been determined, is clear and simple.

(*f*) *Information gained as a Partner.* — Repeated attempts have been made to compel a partner to account to his firm for all profits resulting from his use of the knowledge or skill acquired in the partnership business. Undoubtedly, if a partner acquires information which is the property of the firm, — e. g. news gathered by a newspaper partnership,[3] — "that is to say, information the use of which is valuable to them as a partnership, and to the use of which they have a vested interest,"[4] he will not be permitted to use it for his personal profit. But "to hold that a partner can never derive any personal benefit from the information which he obtains as a partner would be manifestly absurd. Suppose a partner to become, in the course of carrying on his business, well acquainted with a particular branch of science or trade, and suppose him to write and publish a book on the subject, could the firm claim the profits thereby obtained? Obviously not, unless

[1] Northrup *v.* Phillips, 99 Ill. 449 (1881).

[2] Latta *v.* Kilbourn, 150 U. S. 524; 14 Sup. Ct. 201 (1893); Burdick's Cases on Part. 503, reversing the decision of the Supreme Court of the District of Columbia, 5 Mackey, 304 (1886); 7 Mackey, 80 (1888).

[3] Glassington *v.* Thwaites, 1 Sim. & St. 124 (1823).

[4] Bowen, L. J., in Aas *v.* Benham [1891], 2 Ch. 244, 258.

by publishing the book he in fact competed with the firm in their own line of business."[1]

**§ 2. To Devote Themselves to the Business.**

The duty of every partner to devote himself honestly and zealously to the business of the partnership has never been questioned by the courts. Even "an express covenant in partnership articles not to 'engage in any trade or business except upon the account and for the benefit of the partnership,' has been held to add nothing to the duty already imposed by law."[2]

The reasons for prohibiting partners from engaging in another business have been stated by an eminent English judge[3] substantially as follows. It may divert his mind from the partnership business, and take away his time and attention; or it may make him liable for the losses of the other business, and so may involve him and damage the partnership in which he is engaged.

(*a*) *His Liability upon Violating this Duty.* — In case he violates this obligation, without the consent of his copartners, they may intervene by injunction, or may have the partnership dissolved, or, if they can show that the firm has been damaged by his breach of duty or of contract

[1] These remarks of Lindley, L. J., in the last cited case at p. 256 are expressly approved in Latta *v.* Kilbourn, *supra;* Burdick's Cases on Part. at p. 514. They are also in accord with Jennings *v.* Rickard, 10 Col. 395, 400, 401, 15 Pac. 677 (1887), holding that information concerning a mining district, acquired by a partner while prospecting for his firm, if not fraudulently withheld from his firm, could be used for his sole advantage after the dissolution of the partnership; and with Burr *v.* De La Vergne, 102 N. Y. 415, 7 N. E. 366 (1886), holding that inventions made by a partner, although relating to improvements of machinery owned by the firm, are his separate property, unless the making of such inventions is within the scope of the partnership business, or there is an agreement that they shall belong to the firm.

[2] Pollock's Dig. of Part. (6th ed.), 88.

[3] Jessel, M. R., in Dean *v.* MacDowell, 8 Ch. D. 345, 348 (1878).

stipulation on the subject, may recover damages. They are not entitled, however, to any share of the profits of his separate business,[1] unless it is a competitive business in the sense pointed out in a former paragraph, nor do they become joint owners with him of property acquired in that business.[2]

(*b*) *The Copartners' Right to Compensation.*—It follows from the duty resting on each partner, to devote his time and energies to the partnership, that he is not entitled to extra compensation, in the absence of an agreement express or implied securing it to him,[3] although by the sickness[4] or death of a copartner extraordinary responsibility and labor are thrown upon him. Such a risk is incidental to the partnership relation.

The bar to extra compensation by a surviving partner, however, is not an absolute one.[5] "The tendency is to deal with such questions on their particular circumstances, rather than by absolute rules."[6] Moreover, if one partner wilfully withdraws from the business, and casts upon his associates the entire burden of providing capital, labor, and skill, he has no right to complain if the court, upon an accounting, awards to his copartner an extra allowance.[7]

1 Case in last note; Latta *v.* Kilbourn, 150 U. S. 524 (1893); Burdick's Cases on Part. 503, 512.

2 Belcher *v.* Whittemore, 134 Mass. 330 (1883); Burdick's Cases on Part. 515.

3 Askew *v.* Springer, 111 Ill. 662 (1884).

4 Heath *v.* Waters, 40 Mich. 457 (1879).

5 Zell's Appeal, 126 Pa. 329; 17 At. 647 (1889). In this case, the survivor, more than thirteen years after the liquidating partner's death, discovered a firm claim, prosecuted it successfully for four years, and because of the exceptional facts was allowed extra compensation.

6 Thayer *v.* Badger, 171 Mass. 279; 50 N. E. 541 (1898). *Cf.* Pollock's Dig. of Part. § 24 (6), and comments, p. 77 (6th ed.); and Lindley on Part. (6th ed.), 394.

7 Mattingly *v.* Stone's Adm'r, 35 S. W. (Ky.) 921 (1896); Burdick's Cases on Part. 516.

## § 3. To Contribution.

A learned writer has expressed the opinion, that the "duty imposed on the firm to indemnify any one of its members against extraordinary outlays for necessary purposes is one of a class of duties *quasi ex contractu* which are recognized by the law of England only very sparingly and under special circumstances. It is outside the rules of agency, and has still less to do with trust; real analogies are to be found in salvage and average."[1]

(*a*) *Duty of Contribution imposed by the Partnership Contract.*—Judicial authority for this view is not very abundant, and the learned writer admits that eminent judges have based a partner's right to indemnity against extraordinary outlays upon his implied authority to make the expenditures. In the case referred to,[2] Lord Justice Turner held that a partner might be entitled to reimbursement of moneys paid out for his firm, although he could not have subjected it to liability to a third person from whom he had borrowed the money. Borrowing money by the manager of a mining partnership, he said, was not within his implied authority, but paying the necessary expenses of the business was.[3] In his opinion, there was no injustice in holding the partners "liable for wages incurred, and debts contracted for the purposes of the mine, for then they have the benefit of the expenditure."

1 Pollock's Dig. of Part. (6th ed.) 76.

2 Ex parte Chippendale, In re German Mining Co., 4 De G. M. & G. 19, 40 (1853).

3 This appears to be the theory underlying the provision of the British Partnership Act on this topic, § 24 (2): "The firm must indemnify every partner in respect of payments made and personal liabilities incurred by him, (*a*) in the ordinary and proper conduct of the business of the firm; or (*b*) in or about anything necessarily done for the preservation of the business or property of the firm."

This is quite in accord with the doctrine declared in an earlier case,[1] "that a partnership creates an agreement that, in case any partner pays more than his share, the others shall indemnify him." The same doctrine was laid down by Chancellor Kent. After stating that a partner who had paid a firm debt with his own funds was entitled to contribution from his copartner, he added, "This is the intendment in the first instance." [2]

In this country, the right of a partner to contribution has been treated by the courts generally as being within "the rules of agency," [3] and as having, in some cases, a good deal "to do with trust." [4]

(*b*) *May be Modified by Contract.* — Because of "the common saying, that the right to contribution is independent of agreement," Lord Justice Lindley [5] has felt it necessary to call attention to the very obvious fact, that by agreement the partners may limit the right to contribution,[6] or may exclude it altogether.[7]

(*c*) *Incidental to a Partnership Settlement.* — The duty to make contribution is enforceable, as a rule, only after a final settlement of partnership affairs. Until that is made, it is obviously impossible to fix the amount to which the plaintiff partner is entitled. Although he may have paid various sums for the benefit of the firm, a final settlement

1 Wright *v.* Hunter, 5 Ves. 792, 793 (1800).

2 Sells *v.* Hubbell, 2 Johns. Ch. 394, 397 (1817).

3 Meserve *v.* Andrews, 106 Mass. 419 (1871).

4 Lee *v.* Dolan, 39 N. J. Eq. 193 (1884).

5 Lindley on Part. (6th ed.), 372.

6 Scudder *v.* Ames, 89 Mo. 491, 508; 14 S. W. 525 (1886); 142 Mo. 187, 217; 43 S. W. 659 (1897). The agreement was implied from the usages of the partners.

7 McFadden *v.* Lecka, 48 Ohio, 513; 23 N. E. 874 (1891). Managers were forbidden to make contracts or create debts beyond the available capital.

may disclose still larger overdrafts by him, or still larger payments by his copartners.[1]

If, after such a settlement has been made, and the firm assets are exhausted, a partner pays a firm debt, he may bring his action for contribution;[2] and so he may, whenever an accounting is not necessary to determine the amount which each partner should contribute.[3]

The shares payable by each contributory will be considered in a subsequent chapter.[4]

(*d*) *Contribution may be Denied.* — If the outlays for which a partner seeks contribution were not made "in the ordinary and proper conduct of the business of the firm,"[5] his claim for contribution will be denied,[6] unless his acts have been duly ratified by the firm.[7]

This doctrine applies where the plaintiff partner has been compelled to pay damages for fraudulent representations made by him to a purchaser of firm property, without the knowledge or assent of his copartner. A wilful wrongdoer has no right to indemnity from an innocent copartner.[8] Nor, if all of the partners have joined in the commission of a pure tort, or have violated a penal statute, will either be entitled to contribution from the others.[9] "Otherwise 'where the matter is indifferent in itself,' and the wrongful act is not clearly illegal, but may have been done in honest ignorance or in good faith to determine

1 Warring *v.* Arthur, 98 Ky. 34; 32 S. W. 221 (1896); Burdick's Cases on Part. 518.

2 Sears *v.* Starbird, 78 Cal. 225; 20 Pac. 547 (1889).

3 Jepson *v.* Beck, 78 Cal. 540; 21 Pac. 184 (1889).

4 Chap. VIII.

5 British Partnership Act, 1890, § 24 (2) (*a*).

6 Thomas *v.* Atherton, 10 Ch. D. 185 (1877).

7 Cragg *v.* Ford, 1 Y. & C. C. C. 280 (1842).

8 Clayton *v.* Davitt, 56 N. J. Eq. 000; 38 At. 308 (1897); Burdick's Cases on Part. 521.

9 Lindley on Part. (6th ed.), 382.

a claim of right, there is no objection to contribution or indemnity being claimed." [1]

(*e*) *Purchaser of a Partner's Share.* — The duty of contribution does not pass to the purchaser of a partner's share. Undoubtedly the copartner who remains in control of the firm assets may reimburse himself out of their proceeds, and thus diminish the sum going to the purchaser. But, if with full knowledge of all the facts, he pays a sum to the purchaser in full of the assigned share, he cannot thereafter maintain an action against the purchaser for contribution, upon being compelled to pay a claim against the firm. The fact that he believed the claim to be groundless will not avail him. It is at most a case of voluntary payment made under a mistake of law.[2]

### § 4. Actions at Law between Partners.

Partners are not allowed to sue each other at law upon matters which are properly items in the partnership account. In such cases "it would be useless for one partner to recover what, upon taking a general account among all the partners, he might be liable to refund." [3] Moreover, such transactions do not result in one partner becoming a debtor to or a creditor of the others, but his liability or his claim runs to or against the firm.[4] Accordingly, a partner cannot maintain an action at law against his copartners for services [5] rendered or for premises leased to the firm,[6] although the partnership agreement secures to him a fixed sum therefor; nor for damages

[1] Pollock on Torts (5th ed.), 191; Clayton *v.* Davitt, *supra;* Horbach *v.* Elder, 18 Pa. 33 (1851).

[2] Clayton *v.* Davitt, 56 N. J. Eq. 000; 38 At. 308 (1897); Burdick's Cases on Part. 521, 524.

[3] Sadler *v.* Nixon, 5 B. & Ad. 936 (1834).

[4] Ives *v.* Miller, 19 Barb. (N. Y.) 196 (1855).

[5] Causten *v.* Burke, 2 Har. & G. (Md.) 295 (1828).

[6] Estes *v.* Whipple, 12 Vt. 373 (1840).

caused by his copartner's breach of an express covenant to devote his whole time to the partnership;[1] nor for the copartner's breach of his contract to make an annual settlement of accounts and annual payments thereunder;[2] nor for money loaned to or paid for the firm.[3]

(*a*) *Common Law Action of Account.* — Lord Justice Lindley has stated that he knows of no instance of an old common law action of account brought by one partner against another; adding that courts of law had no machinery enabling them to do justice in matters of account.[4] Chancellor Kent declared that "an action of account at law may be brought by one partner against another," and that, as in such an action the auditors could compel the parties to be examined under oath, he had "not been able to discern any good reason why that action has so totally fallen into disuse."[5] Judge Bronson assigned the following reason for its obsolescence: "All the books agree that this is one of the most difficult, dilatory, and expensive actions that ever existed."[6] He said it did not "appear that more than one action of account was ever brought before,[7] and," he added, "the present experiment will probably be the last."

This was a mistaken prophecy. Another experiment was made, but that also resulted in failure, chiefly, however,

[1] Capen *v.* Barrows, 1 Gray (Mass.) 376 (1854).

[2] Ryder *v.* Wilcox, 103 Mass. 24 (1869).

[3] Springer *v.* Cabell, 10 Mo. 640 (1847); White *v.* Harlow, 5 Gray (Mass.) 463 (1855).

[4] Lindley on Part. (6th ed.), 547.

[5] Duncan *v.* Lyon, 3 Johns. Ch. 351 (1818), approved in Wilhelm *v.* Caylor, 32 Md. 157 (1869).

[6] McMurray *v.* Rawson, 3 Hill (N. Y.) 59 (1842). He did not propose to encourage the action by removing any of its difficulties. "If parties chose to bring account," he remarked, "they must take the action as it was left by the ancients."

[7] Jacobs *v.* Fountain, 19 Wend. 121 (1838).

because the firm consisted of three members.[1] In such a case, it was declared that two of the partners "cannot join as plaintiffs, as against the other, because two cannot have a joint right of recovery against the third. And one of them cannot recover against the other two, as co-defendants, because there is no joint liability. Neither can any one of the three recover against either of the others singly, since the mutual claims of any two of them cannot be completely adjusted without deciding upon those of the third."[2]

(*b*) *Modified Forms of Action of Account.*—In some of our States a partner is allowed to maintain an action at law against his copartner, although it involves an inquiry into the partnership accounts, where "the partnership was in a single and completed transaction,"[3] or where the dealings between two partners embrace but a few items, and a settlement of the accounts is simple.[4] Indeed, it has been declared that though the statement of an account between partners might be difficult, resort might be had to a common law action of account, nevertheless, "there being only two partners concerned, and discovery being now obtainable as well at law as in equity."[5]

1. ACTION FOR WRONGFUL OUSTER OF COPARTNER.—In England a partner cannot work a dissolution of the firm by excluding his copartner from participation in the firm business, where the partnership has been entered into for a fixed term, nor can a majority of its members expel a partner, unless the partnership agreement expressly confers the power.[6] Accordingly, a partner who has been wrong-

[1] Appleby *v.* Brown, 24 N. Y. 143 (1861). See dissenting opinion of James, J., p. 147.

[2] Beach *v.* Hotchkiss, 2 Conn. 425 (1818).

[3] Kutz *v.* Dreibelbis, 126 Pa. 335; 17 At. 609 (1889).

[4] Clarke *v.* Mills, 36 Kan. 393; 13 Pac. 569 (1887).

[5] Wheeler *v.* Arnold, 30 Mich. 304, 306 (1874).

[6] British Partnership Act, §§ 24 (5), 25.

fully ousted from the partnership should proceed against his copartner, not for damages, but for "reinstatement in his rights as a partner."[1]

In this country, a partner who has been excluded wrongfully from the partnership may recover in an action at law damages against his former copartners for their breach of the partnership contract;[2] or he may compel them to account in equity for the profits of the business carried on with the partnership property, subject to proper allowances.[3]

(*a*) *Action for Refusal to Launch a Partnership.* — If no partnership business has been transacted, and no accounting is necessary to adjust the rights of the partners, an action at law for damages may be maintained by a partner, who was ready and willing to carry out the contract, against his co-partner for preventing the launching of the partnership.[4]

2. Actions which do not Involve Partnership Accounts. — (*a*) *Voluntary Settlement between the Partners.* — If the members of a firm have settled its affairs, and have agreed upon the balance due from one to the other, an action at law may be maintained therefor.[5] If, however, they have gone no further than to state the account between the firm and its members, an action at law will not lie between them. Such an account would show the indebtedness of the several partners to the firm, or its indebtedness to them, but would not furnish evidence of

[1] Pollock's Dig. of Part. (6th ed.), 80, citing Wood *v.* Wood, L. R. 9 Ex. 190 (1874), and Blisset *v.* Daniel, 10 Ha. 493 (1853).

[2] Hunter *v.* Land, 81* Pa. 296 (1875).

[3] Karrick *v.* Hannaman, 168 U. S. 328, 337; 18 Sup. Ct. R. 135 (1897).

[4] Hill *v.* Palmer, 56 Wis. 123; 43 Am. R. 703 (1882); and cases cited.

[5] Wray *v.* Milestone, 5 M. & W. 21 (1839).

an agreement that any partner was to pay to another a stipulated sum.[1]

When the partnership relates to a single transaction, for example, the sale of particular mining property, and it is agreed that the partners shall share equally in the commissions received on the sale, an accounting is unnecessary, and an action at law for his share may be maintained by a partner against the copartners who have received and retained the whole sum.[2]

(b) *Agreements antecedent to the Partnership.* — It often happens during the negotiations for a partnership that one of the parties loans to another his share of the firm capital,[3] or that they join in a note upon which they raise the money which they are severally to put into the business, and one of them is compelled to pay the entire note.[4] In such cases, the claim of the creditor against the debtor cannot be made an item in the partnership accounts without the subsequent consent of all the partners. Accordingly, it may be recovered in an action at law, even during the continuance of the partnership.

(c) *Insulated Agreements.* — It is entirely competent for partners to make "special bargains by which particular transactions are insulated and separated from the winding up of the concern, and are taken out of the general law of partnership."[5] Of such bargains, the following are examples. One partner agrees to pay his copartner a stipulated sum for the latter's interest in certain partnership chattels.[5] One partner promises to pay another partner a fixed sum

[1] Ross *v.* Cornell, 45 Cal. 133 (1872); Arnold *v.* Arnold, 90 N. Y. 580 (1882).

[2] Mason *v.* Sieglitz, 22 Col. 320; 44 Pac. 588 (1896); Burdick's Cases on Part. 537.

[3] Venning *v.* Leckie, 13 East, 7 (1810); Haskins *v.* Curran, 43 Pac. (Idaho) 559 (1895); Burdick's Cases on Part. 534.

[4] Halleck *v.* Streeter, 73 N. W. (Neb.) 219 (1897).

[5] Bayley, B., in Jackson *v.* Stopherd, 2 Cr. & M. 361 (1834).

for his personal attention to the affairs of the firm.[1] One or more partners give a promissory note to another for his share in the profits[2] or in the assets[3] at a particular time. One partuer binds himself to a copartner "to keep the books of the firm in a careful and workmanlike manner, and to render a just, true, and accurate account of all" the partnership business.[4]

In these cases, and all similar ones, the contract is between the partners as individuals. The partnership, it is true, furnishes the occasion for the agreement, but the firm is not a party to the contract. Hence, an action for its breach in no way involves the partnership accounts.

(*d*) *Wrongful Use of Firm Property.* — As each partner has authority to use the firm property, and even to dispose of it in the ordinary course of the business, his negligent use of it does not give his copartners a right of action for damages against him; nor does his failure to account for the proceeds of property which he sells. Such matters are properly adjusted upon an accounting. But if he actually ousts his copartners from firm realty, they can maintain an action at law against him.[5] So they may if he wrongfully sells the firm property as his own, and converts the proceeds to his use;[6] or if he issues negotiable paper in the firm name for his personal benefit, which his copartners are compelled to pay;[7] or if he makes a fraudulent

[1] Paine *v.* Thacher, 25 Wend. (N. Y.) 450 (1841).

[2] Sturges *v.* Swift, 32 Miss. 239 (1856).

[3] Wilson *v.* Wilson, 26 Or. 251; 38 Pac. 185 (1894); Burdick's Cases on Part. 538.

[4] McCauley *v.* Cooley, 45 Neb. 582; 63 N. W. 871 (1895); Burdick's Cases on Part. 535.

[5] Doe *v.* Horn, 5 M. & W. 564 (1839); Lindley on Part. (6th ed.), 549.

[6] Morris *v.* Wood, 35 S. W. 1013 (Tenn.) (1896); Burdick's Cases on Part. 531.

[7] Fuller *v.* Percival, 126 Mass. 381 (1879).

settlement of a firm claim, thereby causing damage to his partners;[1] or if he fraudulently diverts firm funds from the payment of firm debts to the payment of his individual indebtedness.[2]

Some of the cases cited in the last four notes were not actions at law; but the principles which they enunciate are fairly stated in the preceding paragraph.[3] A partner who, in Lord Eldon's language, "may be represented as having stolen property out of the joint fund,"[4] has no right to insist that his copartners content themselves with charging its value against him in the firm accounts.

(*e*) *Tortious Conduct toward a Copartner.* — The existence of partnership relations between the plaintiff and the defendant is no bar to an action for a personal wrong done by the defendant to the plaintiff. If a partner violently thrusts his copartner from the place of business of the firm, and threatens the latter's life if he returns, the latter may have him put under bonds to keep the peace.[5] So a partner may maintain an action at law against a copartner who wrongfully injures the plaintiff's separate property, although it was at the time in the possession and use of the partnership.[6] He may maintain such an action also for fraudulent representations made to him by the defend-

[1] Sweet *v.* Morrison, 103 N. Y. 235; 8 N. E. 396 (1886). In this case plaintiff charged his four copartners and a firm debtor with fraudulently settling a firm claim. The court held that he could not recover the firm debt, for that was discharged by the act of the four; but if he could show a fraudulent settlement, his damages would be measured by the diminution of his partnership share produced by a collusive waste of partnership assets.

[2] Patrick *v.* Weston, 22 Col. 45; 43 Pac. 446 (1895); Burdick's Cases on Part. 529.

[3] See Lindley on Part. (6th ed.), 549.

[4] Ex parte Yonge, 3 V. & B. 31 (1814).

[5] Regina *v.* Mallison, 16 Ad. & E. N. S. 367 (1851).

[6] Newby *v.* Harrell, 99 N. C. 149 (1888); Burdick's Cases on Part. 543.

ant upon a sale of the latter's interest to him,[1] or upon the formation of the partnership.[2]

3. ACTIONS BETWEEN FIRMS HAVING A COMMON MEMBER. — These could not be maintained at common law. Various reasons were assigned for the doctrine. It was said that no legal contract could subsist between the common member and his copartners on the one side and himself with his other copartners on the other side, although they could so far enter into the contract as to render it available in equity.[3] It was also declared that all the partners must join and be joined in the action, and that the common member could not be at the same time both a plaintiff and a defendant.[4]

Under the reformed procedure prevailing in most of our States [5] and in England,[6] these technical objections have no longer any force. The fact that a partner in the plaintiff firm is also a member of the defendant firm, will not prevent either firm from maintaining an action at law

[1] Glade *v.* White, 42 Neb. 336; 60 N. W. 556 (1894); Burdick's Cases on Part. 541.

[2] Hale *v.* Wilson, 112 Mass. 444 (1873). "The gist of the plaintiff's case is that there was no real partnership formed; that agreement to form a partnership was a pretence used by the defendant to defraud the plaintiff of his money, and that the money was not used, or intended to be used, for partnership purposes."

The British Partnership Act of 1890, § 41, entitles the defrauded partner, upon the rescission of the partnership, (*a*) "to a lien on or right of retention of the surplus of the partnership assets, after satisfying the partnership liabilities, for any sum of money paid by him for the purchase of a share in the partnership, and for any capital contributed by him; (*b*) to stand in the place of the creditors of the firm for any payments made by him in respect of the partnership liabilities; and (*c*) to be indemnified by the person guilty of the fraud or making the representation against all the debts and liabilities of the firm."

[3] Bosanquet *v.* Wray, 6 Taunt. 597 (1815).

[4] Beacannon *v.* Liebe, 11 Or. 443 (1884).

[5] Crosby *v.* Timolat, 50 Minn. 171; 52 N. W. 526 (1892).

[6] Lindley on Part. (6th ed.), 276, 277.

against the other. All of the parties being before the court, "it will proceed to pronounce such judgment as the facts of the case require." Even though an account may be necessary in order to determine the equitable rights of the individual parties, the better doctrine is "to let the debtor firm pay its debt, and the creditor firm, after receiving its debt, adjust their individual equities among themselves."[1]

(*a*) *Actions between a Partnership and a Partner.* — Here again common law technicalities operated to defeat the plaintiff. If, however, a firm gave its negotiable note or bill to a partner, or *vice versa*, the payee could negotiate the instrument and give to his transferee a right of action against the maker.[2] The same result follows from an assignment of his claim against the firm by a partner, or of its claim against a partner by the firm, in a jurisdiction where the assignee of a chose in action may sue in his own name.[3]

Under the reformed procedure in some of our States,[4] and under legislation in others declaring the contracts of a firm to be the joint and several contracts of its members,[5] it is possible for a partner to maintain an action at law against his copartners on a firm indebtedness to him.

[1] Cole *v.* Reynolds, 18 N. Y. 74 (1858); Burrows *v.* Leech, 74 N. W. (Mich.) 296 (1898).

[2] Pitcher *v.* Barrows, 17 Pick. (Mass.) 361 (1835).

[3] Frank *v.* Anderson, 13 Lea (Tenn.) 695 (1884).

[4] Stettheimer *v.* Tone, 114 N. Y. 501, 505; 21 N. E. 1018 (1889). The partner's claim here was that of a depositor in a bank owned by his firm.

[5] Willis *v.* Barron, 143 Mo. 450; 45 S. W. 289 (1898). In this case it was also held that defendants could not plead as a counter claim an unliquidated partnership account. In order "to oust a court of law of jurisdiction, a party must go further and state some specific ground for invoking the jurisdiction of equity."

# CHAPTER VII.

## DISSOLUTION OF PARTNERSHIPS.

### § 1. By Operation of Law.

A PARTNERSHIP may be dissolved without the assent of the parties and without a judicial decree. Upon "the happening of any event which makes it unlawful for the business of the firm to be carried on, or for the members of the firm to carry it on in partnership," the firm is dissolved by operation of law.[1] If a partnership exists between a citizen of Great Britain and a citizen of the United States, it is at once dissolved upon the breaking out of war between the two countries. Not only is the continuance of the partnership thereafter inconsistent with the allegiance which each partner owes to his country, but if the business includes commercial transactions between the two countries, the war puts them under the ban. As one of the main purposes for which the partnership was organized has thus become legally unattainable, it would be unjust for the law to continue the partnership relation.[2]

In a jurisdiction where a judge is absolutely prohibited from practising law in any court, a partnership of attorneys is dissolved by the appointment and qualification of one of its members as a judge.[3]

(*a*) *By the Death or Bankruptcy of a Partner.* — "Subject to any agreement between the partners, every

[1] British Partnership Act of 1890, § 34.

[2] Griswold v. Waddington, 15 Johns. N. Y. 57 (1818); 16 Johns. 438; Burdick's Cases on Part. 544.

[3] Justice v. Lairy, 49 N. E. 459; 19 Ind. App. 272 (1898).

partnership is dissolved as regards all the partners by the death or bankruptcy of any partner." [1]

Either of these events must necessarily dissolve the firm, so far as the decedent's or bankrupt's estate is concerned; for that passes by operation of law to his personal representative or his trustee, neither of whom has a right to enter the firm without the consent of the other partners, nor is either bound to become a partner without his own consent.

Either of these events must operate also to dissolve the partnership as between the surviving partners, unless they have agreed [2] that it shall not have that effect. "The *delectus personarum* lies at the foundation of the agreement of the parties, and is one of the main considerations on which it rests. The personal qualities of each member of a firm enter largely into the inducements which lead parties to form a copartnership; and if the abilities and skill or the character and credit of any one are withdrawn the contract between them is terminated and the copartnership is dissolved." [3]

Moreover, as the death or bankruptcy of a partner is a public fact, every one is bound in law to take notice of it; and consequently any new contract entered into by a survivor in the name of the firm, but without the knowledge or consent of his copartners, will bind him only, even though he and the other contracting party were in fact ignorant of the firm's dissolution.[3]

(*b*) *By the Marriage of a Female Partner.* — At common law the share of a *feme sole* in a partnership passed

[1] British Partnership Act of 1890, § 33 (1).

[2] Shaw *et al.*, Appellants, 81 Me. 207; 16 At. 662 1889; Carter *v.* McClure, 98 Tenn. 109; 38 S. W. 585 (1897); Burdick's Cases on Part. 37, 40.

[3] Marlett *v.* Jackman, 3 Allen (Mass.) 257 (1861); Burdick's Cases on Part. 547.

to her husband upon marriage, and her legal personality for many purposes became merged in his. It followed that her marriage produced an instantaneous dissolution of a partnership in which she was a member.[1] Under the Married Women's Property Act in Britain, and similar legislation in many of our States, the marriage of a female partner "no longer causes the dissolution of a partnership."[2]

### § 2. Dissolution by Act of the Parties.

The partners may stipulate in their original contract that the partnership shall continue for a fixed term. In such case, it will be dissolved by the expiration of that term.[3] If, however, the parties go on in business after the stipulated period, but "without any express new agreement, the rights and duties of the partners remain the same as they were at the expiration of the term, so far as is consistent with the incidents of a partnership at will."[4]

By mutual consent the partners may dissolve the partnership at any moment; and this consent may be express[5] or implied.[6]

(*a*) *A Particular Adventure.* — If a partnership is formed for a single adventure or undertaking, its dissolution occurs with the completion of the contemplated

[1] Nerot *v.* Burnand, 4 Russ. 247, 260 (1827); Bassett *v.* Shepardson, 52 Mich. 3; 17 N. W. 217 (1883); Burdick's Cases on Part. 553; Brown *v.* Chancellor, 61 Tex. 437, 445 (1884).

[2] Lindley on Part. (6th ed.), 575; Burney *v.* Savannah Grocery Co., 98 Ga. 711; 25 S. E. 915 (1896); Burdick's Cases on Part. 11.

[3] British Partnership Act of 1890, § 32 (*a*).

[4] British Partnership Act of 1890, § 27 (1).

[5] Bank of Montreal *v.* Page, 98 Ill. 109 (1881).

[6] Kennedy *v.* Porter, 109 N. Y. 526, 551; 17 N. E. 476 (1888). By the return of the original capital to the several partners and the final distribution of the assets.

business.[1] In accordance with this rule, it has been held that the organization of a corporation works the instant dissolution of a partnership whose articles provided that the firm should be incorporated "as soon as may be."[2]

(*b*) *Partnerships at Will.* — If the term of the partnership is not fixed either expressly or by implication, it may be terminated at the will of either partner by giving notice to his copartners of his intention to dissolve it. The British Partnership Act provides that in such a case "the partnership is dissolved as from the date mentioned in the notice as the date of dissolution, or if no date is so mentioned, as from the date of the communication of the notice."[3] Such appears to be substantially the rule recognized by our courts.[4] As the consent of the other partners to the dissolution is unnecessary, the insanity of the partner to whom the notice is given is immaterial.[5] After a valid notice has been given, the consent of all the partners is necessary to its retraction.[6]

1. Partnerships for a Fixed Term. — Whether a partnership, which the parties have agreed shall continue for a definite period, can be dissolved by the act of one partner without his copartner's consent, is a question upon which there is much difference of opinion.

(*a*) *The English Doctrine.* — It appears to be settled in England that it cannot be thus dissolved. A partner, as we have seen,[7] cannot be expelled from such a partnership, unless the partnership articles confer the power of

[1] British Partnership Act of 1890, § 32 (*b*); Boher *v.* Drake, 33 Minn. 408; 23 N. W. 840 (1885).

[2] Hennessy *v.* Griggs, 1 N. Dak. 52, 59; 44 N. W. 1010 (1890).

[3] § 32 (*c*).

[4] Fletcher *v.* Reed, 131 Mass. 312 (1881); Burdick's Cases on Part. 554; Green *v.* Waco State Bank, 78 Tex. 2 (1890).

[5] Mellersh *v.* Keen, 27 Beav. 236 (1859).

[6] Jones *v.* Lloyd, L. R. 18 Eq. 265 (1874).

[7] *Supra*, p. 319; *cf.* Barnes *v.* Young [1898]; 1 Ch. 414.

expulsion upon his associates; nor can he, by attempting to withdraw from the firm, break it up. Neither can he by suffering his share to be charged with the lien of a judgment, nor by assigning his share, force the purchaser or assignee into the firm, or confer upon such purchaser or assignee the right to call the other partners to an account.[1] Such conduct does give to his copartners, however, the right to have the partnership dissolved by judicial decree.[2]

(*b*) *Different Views in this Country.* — The English doctrine appears to be sound in principle; and it has received the approval of distinguished writers, as well as of a few courts in this country.[3] However, the weight of judicial authority, in both the Federal and the State courts, is opposed to that doctrine.[4]

In a recent case,[5] the United States Supreme Court states the principal reasons for the prevailing view in this country, as follows: "A contract of partnership is one by which two or more persons agree to carry on a business for their common benefit, each contributing property or services, and having a community of interest in the profits. It is, in effect, a contract of mutual agency, each partner acting as a principal in his own behalf and as agent for his copartner. Every partnership creates a personal rela-

[1] British Part. Act of 1890, §§ 24 (7), 31, 32; Brown *v.* Hutchinson [1895], 2 Q. B. 126; Burdick's Cases on Part. 419; Lindley on Part. (6th ed.), 563, 575.

[2] British Part. Act of 1890, §§ 33 (2), 35.

[3] Ferero *v.* Buhlmeyer, 34 How. Pr. (N. Y.) 33 (1867); Hannaman *v.* Karrick, 9 Utah, 236; 33 Pac. 1039 (1893); Story on Part. (6th ed.) § 275.

[4] Solomon *v.* Kirkwood, 55 Mich. 256; 21 N. W. 336 (1884); Burdick's Cases on Part. 554; 3 Kent's Comm. (14th ed.), *54.

[5] Karrick *v.* Hannaman, 168 U. S. 335; 18 Sup. Ct. R. 135 (1897), refusing to assent to the opinion of the court below (9 Utah, 236, *supra*), that "a partnership for a definite time cannot be dissolved by one partner at his own will and without the consent of his copartner, within that time."

tion between the partners, rests upon their mutual consent, and exists between them only. Without their agreement or approval, no third person can become a member of the partnership, either by act of a single partner or by operation of law; and the death or bankruptcy of a partner dissolves the partnership. So, an absolute assignment by one partner of all his interest in the partnership to a stranger dissolves the partnership, although it does not make the assignee a tenant in common with the other partners in the partnership property. No partnership can efficiently or beneficially carry on business without the mutual confidence and co-operation of all the partners. Even when, by the partnership articles, they have covenanted with each other that the partnership shall continue for a certain period, the partnership may be dissolved at any time, at the will of any partner, so far as to put an end to the partnership relation, and to the authority of each partner to act for all, but rendering the partner who breaks his covenant liable to an action at law for damages, as in other cases of breaches of contract."

(*c*) *Dissolution in Breach of Contract, causing Damage.* — According to this view, a stipulation in a partnership contract that the relation shall continue for a fixed period, has this effect only: it entitles the non-consenting partners to such damages as they can show they have sustained by the breach of the agreement.[1]

In Solomon *v.* Kirkwood, it is intimated that "there may be cases in which equity would enjoin a dissolution for a time, where the circumstances are such as to make it specially injurious"; but in Karrick *v.* Hannaman, it is declared that, while equity "will not assist the partner breaking his contract to procure a dissolution, . . . generally speaking, neither will it interfere at the suit of the other partner to prevent dissolution, because while it may

[1] Cases cited in the last two notes. California Civil Code, § 2451.

compel the execution of articles of partnership so as to put the parties in the same position as if the articles had been executed as agreed, it will seldom, if ever, specifically compel subsequent performance of the contract by either party, the contract of partnership being of an essentially personal character."

**§ 3. Dissolution by the Court.**

Allusion has been made to some of the causes for which a court of equity will decree the dissolution of a partnership. Fraud, practised by the defendant on the plaintiff, which induced the latter to enter into the relation, may, as we have seen, authorize a decree annulling the partnership.[1] Suffering his share to be charged or seized under a separate judgment against him, or the sale and assignment of his share without his partner's consent,[2] will justify his copartner in bringing a suit in equity for a dissolution. Let us now consider the other causes for which dissolution may be decreed.

(*a*) *Lunacy of a Partner.* — There is some authority for the proposition that a judicial declaration of the lunacy of a partner works the immediate dissolution of the partnership, because it "suspends the whole functions and rights of the party to act personally."[3] It is held generally, however, both in England and in this country, that the lunacy of a partner does not of itself produce a dissolution, although it is a valid reason for dissolution by the court upon the application of the sane partner, or on behalf of the insane partner.[4]

[1] *Supra*, p. 324. Oteri *v.* Scalzo, 145 U. S. 578; 12 Sup. Ct. R. 895 (1892).

[2] *Supra*, p. 330.

[3] Story on Part. (6th ed.) § 295; Isler *v.* Baker, 6 Humph. (Tenn.) 85 (1845).

[4] Jurgens *v.* Ittmann. 47 La. Ann. 367; 16 So. 952 (1895); Burdick's Cases on Part. 558; British Part. Act of 1890, § 35 (*a*).

This is clearly the better view. As insanity renders its victim incapable of performing his duties as a partner, it furnishes a good ground for dissolution. But unless an application is made for a dissolution, it is fair to presume that the sane partner and those interested in the estate of the insane partner are content that the partnership should continue, in the expectation that the sufferer may recover from his malady.[1]

(*b*) *Permanent Incapacity.* — Whenever a person becomes "permanently incapable of performing his part of the partnership contract," [2] the same principle upon which a dissolution is decreed in case of insanity justifies a court in dissolving the firm, upon the application of the other partner.[3]

(*c*) *Misconduct of a Partner.* — While a court of equity will not decree a dissolution of a partnership for trifling reasons, nor encourage partners in bringing their petty disputes to it for settlement, it will entertain a suit for dissolution against a partner whose misconduct "is calculated to prejudicially affect the carrying on of the business," or which renders the successful conduct of the business by his copartners impracticable.[4]

Hence, a bill will not be dismissed on demurrer which charges the defendant with wilfully and persistently neglecting to comply with the terms of the partnership contract.[5] A partner who fails or refuses to advance the

[1] Raymond *v.* Vaughan, 128 Ill. 256; 15 Am. St. R. 112; 4 L. R. A. 440 (1889).

[2] British Part. Act of 1890, § 35 (*b*).

[3] Whitwell *v.* Arthur, 35 Beav. 140. Paralytic attack. As the evidence indicated that defendant's incapacity was but temporary, dissolution was not decreed, but "proceedings were stayed with leave to apply."

[4] British Part. Act of 1890, § 35 (*c*) and (*d*). California Civil Code, § 2452 (2).

[5] Rosenstein *v.* Burns, 41 Fed. 841 (1882); Burdick's Cases on Part. 557.

money required by the partnership articles subjects himself to a suit for dissolution.[1] So does a partner who insists upon selling spirituous liquors as a part of the firm business, when the partnership contract provides the firm shall not sell such liquors.[2] The same is true of a partner who is shown to have resolved "to break up and ruin the business of the firm," and whose personal relations with his copartners "are such that they can never carry on the business together to advantage."[3]

(*d*) *A Losing Business.* — Even though there be no misconduct on the part of the members and no unpleasant personal relations between them, if a partner can show that the business "can only be carried on at a loss," he is entitled to a decree of dissolution.[4]

(*e*) *For Just Cause.* — After enumerating the foregoing causes for the dissolution of partnerships by judicial decree, the British statute adds: "Whenever in any case circumstances have arisen which, in the opinion of the court, render it just and equitable that the partnership be dissolved,"[5] the court may decree a dissolution.

This clause, it has been suggested, "will be limited in its application to cases *ejusdem generis* as those mentioned in the previous parts of the section; but," the writer adds, "the court ought not to fetter itself by any rigid rules; and any case in which it is no longer reasonably practicable to attain the object with a view to which the partnership was entered into, or to carry out the partnership contract according to its terms, will, it is apprehended, be within this section."[6]

[1] Turnipseed *v.* Goodwin, 9 Al 370 (1846).

[2] Abbott *v.* Johnson, 32 N. H. 9 (1855).

[3] Sutro *v.* Wagner, 23 N. J. Eq. 388 (1873).

[4] Holladay *v.* Elliott, 9 Or. 84 (1879); Rosenstein *v.* Burns, 41 Fed. 841 (1882); Burdick's Cases on Part. 557; British Part. Act of 1890, § 35 (*e*); California Civil Code, § 2452 (3).

[5] British Part. Act of 1890, § 35 (*f*).

[6] Lindley on Part. (6th ed.), 574, 575.

Under a similar provision of the Louisiana statute,[1] it has been held that, as the legislature did not furnish an interpretation of the term "just cause for a dissolution," "it is a question for the court to determine for itself in any given case"; and that as "partnership is essentially a relation of mutual trust and confidence," when they cease, a just cause for dissolution exists.[2] Such appears to be the generally accepted doctrine in this country.[3]

[1] Revised Civil Code, Art. 2887.

[2] Breaux *v.* Le Blanc, 50 La. Ann. 244; 23 So. 281 (1898).

[3] Moore *v.* Price, 116 Al. 247; 22 So. 531 (1897).

# CHAPTER VIII.

## ACCOUNTING AND DISTRIBUTION.

### § 1. The Right to an Accounting.

We have seen that each partner owes to his associates the duty of rendering "true accounts and full information of all things affecting the partnership," including secret profits derived by him at the expense of the partnership.[1] If he fails to perform this duty, his associates are entitled to maintain a suit for an accounting against him.

(*a*) *During the Continuance of the Partnership.* — Generally, such a suit is brought only upon the dissolution of the firm or with a view to a dissolution; ~~but it is~~ now well settled, both in England and in this country, that the suit will lie in some cases, even though a dissolution is not sought. It may be maintained for the recovery of secret profits which the defendant is withholding from his firm;[2] also, when the defendant is attempting to expel or exclude the plaintiff from the partnership,[3] or when the partnership agreement calls for settlements during the continuance of the firm,[4] even though the plaintiff does not ask to have the affairs of the firm wound up.

(*b*) *Right to Accounting not a Test of Partnership.* — Lord Eldon declared[5] that if a person "agrees for a part of the profits, as such, giving him a right to an account,

[1] *Supra,* Chap. VI.
[2] Beck *v.* Kantorowicz, 3 K. & J. 230 (1857).
[3] Richards *v.* Davies, 2 R. & M. 347 (1831).
[4] Patterson *v.* Ware, 10 Ala. 444, 449 (1846).
[5] Ex parte Hamper, 17 Ves. 403, 413 (1811).

though having no property in the capital, he is, as to third persons, a partner." This view is not in accordance with the modern definition of a partnership.[1] It often happens that a person has a right to an accounting, although he is not a partner of the defendant in the business, to which the accounting relates.

If, while negotiations are in progress for a partnership between several persons, property of A is put into the possession of B and C to be used in the business of the contemplated partnership, and it is used by them and they realize a profit therefrom in the business, but a partnership is never perfected, A may maintain a suit for an accounting against B and C "upon principles analogous to those adopted in winding up a common law partnership."[2]

It is also held in this country, that, although a partnership for a fixed term may be dissolved by one partner without the consent of his copartner, the partner who after such a dissolution "carries on the business with the partnership property, is liable, at the election of the other partner or his representative, to account for the profits thereof, subject to proper allowances."[3]

We have seen, that it is also held by many courts in this country that the transferrer of a partner's share and even a sub-partner[4] may maintain a suit for an accounting. Such a plaintiff is not recognized by these courts as a partner, however, and his claim is subject to any defences available against the partner from whom he derives his interest.

(c) *Right to an Accounting not easily lost by a Partner.* — Equity favors the exercise of this right by a

[1] *Ante*, Chap. II. § 3.

[2] Stringfellow *v.* Wise (Va.), 27 S. E. 432 (1897).

[3] Karrick *v.* Hannaman, 168 U. S. 328; 18 Sup. R. 135 (1897).

[4] Nordlinger *v.* Bernheimer, 133 N. Y. 45; 30 N. E. 561 (1892).

partner. It is no answer to a bill for an account, that, upon the dissolution of a partnership between the parties, it was agreed that the defendant should receive all the assets and settle all the affairs of the firm, and that defendant has paid, in settling the affairs, much more than he has received from the assets.[1] Nor is it an answer, that the parties had largely settled their affairs before the commencement of the suit, and that plaintiff was authorized by the defendant to liquidate the business. "Each partner has a right to an accounting from his copartner as to all dealings and transactions connected with the business of the firm, and, as the result may indicate, either to a ratable distribution of any surplus there may be after payment of the debts, or to a ratable contribution to make up the sum required to discharge the debts. Thus all the obligations, both express and implied, arising from the copartnership agreement, may be enforced in a convenient and effective manner, by a court having power to adapt its action to every variety of circumstances."[2]

§ 1. (A.) **Rules of Distribution.**

In the absence of any agreement between the partners on the subject, the rules governing the distribution of firm assets, upon a final settlement of the partnership accounts, are stated as follows in the British Partnership Act:

"(*a*) Losses, including losses and deficiencies of capital, shall be paid first out of profits, next out of capital, and lastly, if necessary, by the partners individually in the proportion in which they were entitled to share profits. (*b*) The assets of the firm, including the sums, if any, contributed by the partners to make up losses or deficiencies of capital, shall be applied in the following manner and order: (1) In paying the debts and liabilities of the firm

[1] Sharp *v.* Hibbins, 42 N. J. Eq. 543; 9 At. 113 (1887).

[2] Watts *v.* Adler, 130 N. Y. 646; 29 N. E. 131 (1891).

to persons who are not partners therein; (2) In paying to each partner ratably what is due from the firm to him for advances as distinguished from capital; (3) In paying to each partner ratably what is due from the firm to him in respect of capital; (4) The ultimate residue, if any, shall be divided among the partners in the proportion in which profits are divided." [1]

1. MODIFIED BY AGREEMENT. — The partnership articles or subsequent agreements between the partners may contain provisions which modify these rules in one or more respects. For example, it may be provided [2] that the contributions by the partners to the firm stock shall not be deemed capital to be repaid by the partnership to the contributors, but firm assets to be distributed upon settlement as profits. In such a case, the court will not treat these contributions as debts due from the firm to the several partners, either in respect of capital, or in respect of advances.

Or it may be provided that the yearly profits shall be added to the capital, instead of accumulating in a separate fund; in which case, after paying outside debts and reimbursing the partners for any advances made by them, the balance of the firm assets will be divided among the partners in payment of the sums due to each in respect of his capital.[3] Such a provision works a material change in the distributive shares of the partners, whenever the proportion in which profits are to be divided is different from the ratio existing between their capitals.

[1] Partnership Act of 1890, § 44.

[2] Groth *v.* Kersting, 23 Col. 213; 47 Pac. 393 (1896); Burdick's Cases on Part. 563.

[3] Molineaux *v.* Raynolds, 54 N. J. Eq. 559; 35 At. 536 (1896); Burdick's Cases on Part. 169; Binney *v.* Mutrie, 12 App. Cas. 160 (1886). The form of the order in the latter case, at pp. 165 and 166, will repay a careful examination.

In Molineaux *v.* Raynolds, referred to in the last note, it reduced the plaintiff's share from about eighteen per cent to about sixteen per cent; and in Binney *v.* Mutrie, it depleted the plaintiff's claim, not only in respect of his share of the assets at the time of distribution, but also in respect of his loss of capital.

2. The Burden of Losses. — According to the rules stated above, this is to be borne ultimately by the partners in the proportion in which they are entitled to share profits, unless they have agreed upon a different proportion. Each partner has the right to insist, however, as against his copartners, that before he contributes from his private means to the satisfaction of such losses, not only shall all profits made in prior transactions be exhausted, but his associates shall pay into the partnership fund every debt due from either of them, whether on account of capital [1] which they have failed to contribute, or on account of overdrafts by them.[2]

3. Illegal Partnerships. — The rules which we have been considering will not be applied in an action for an accounting between members of an illegal partnership. Indeed, an action for an accounting between such partners will not be entertained by the courts.[3] The illegality of the partnership need not be set up by the defendant. If it appears at any stage of the litigation, the court may "refuse to aid either party and leave them where they had placed themselves. . . . To hold otherwise would subordinate the courts to the ingenious devices of men engaged in illegal and even criminal transactions, and compel them to carry out in the solemn forms of law, and

[1] Sangston *v.* Hack, 52 Md. 173 (1879).

[2] Neudecker *v.* Kohlberg, 3 Daly (N. Y.), 407 (1871).

[3] Everett *v.* Williams (1725), 1 European Mag. 360; 9 L. Q. R. 197. Bill in equity for an account by a highwayman against his partner.

by its resistless power, transactions which the same law had pronounced criminal and void."[1]

If, however, the plaintiff is not asking for an accounting by his associate in the illegal partnership, and does not require the aid of the partnership contract to make out his case, but is seeking to enforce an obligation which is supported by an independent consideration, although indirectly connected with the illegal partnership, he may be able to recover.[2]

§ 2. **Repaying Advances.**

A partner who makes advancements to a firm, during its existence or in winding up its affairs, becomes, as against his copartners, a creditor of the firm. He is not in the position of a volunteer. His interest in the firm property and his liability for its debts entitle him to make the advances, and to call on the firm and his associates for reimbursement. Moreover, this reimbursement is to be made before his associates are entitled to repayment on account of their capitals, for, as already stated, his advancement is a loan to the firm, and not an increase of its capital.

After outside debts are satisfied, the advances which have been made by partners are to be repaid in full, if the firm assets are sufficient therefor. In Leserman *v.* Bernheimer,[3] the firm funds, after paying all the liabilities of

[1] Wright *v.* Cudahy, 168 Ill. 86; 48 N. E. 39 (1897); Burdick's Cases on Part. 568, 570; Morrison *v.* Bennett, 20 Mont. 560; 52 Pac. 553 (1898).

[2] Armstrong *v.* Am. Exch. Bank, 150 U. S. 433, 469; 14 Sup. Ct. 186 (1890), thus explaining Brooks *v.* Martin, 2 Wall. 70 (1863); Lindley on Part. (6th ed.) 114; *cf.* Patty-Joiner Co. *v.* City Bank, 41 S. W. (Tex. Civ. App.) 173 (1897); Burdick's Cases on Part. 484.

[3] Leserman *v.* Bernheimer, 113 N. Y. 39; 20 N. E. 869 (1889); Burdick's Cases on Part. 565.

the firm to outsiders, were $128,920. The three partners had contributed $75,000 of capital each, and were to share the profits and losses equally. Bernheimer had advanced for the use of the firm $56,621.39, while his copartners had advanced nothing, but on the other hand had drawn out large sums over and above their shares of the yearly profits. Upon an accounting before a referee, the rules which have been stated in this chapter were not observed. The referee gave to each partner one third of the $128,920, because they had contributed equally to the original capital, and then gave judgment to Bernheimer against each of his copartners for one third of the $56,621.39, thus compelling him to lose one third of the advances which he had made, and throwing upon him the risks of collecting the several judgments from his copartners. The decision was reversed in the Court of Appeals, where the rules above stated were recognized and applied. Bernheimer's advance was declared to be a debt due from the firm, which was to be paid out of the surplus, before any division was made of the partnership capital.

(*a*) *Interest on Advances.* — The partner making advances will be allowed interest thereon, if there is an express agreement to that effect, or if such an agreement can be implied from the circumstances of the case, including trade usages applicable to the particular partnership. Whether he can recover interest, in the absence of such an express or implied agreement, is a question upon which the American courts are divided.

On the one hand, it is said that interest ought not to be allowed because such advances are only items in a fluctuating account, and not separate and distinct loan transactions.[1] On the other hand, it is contended that such advances are loans, especially if made with the knowledge

[1] Prentice *v.* Elliott, 72 Ga. 154, 157 (1883).

of the copartners, and should bear interest at the statutory or customary rate.[1]

In Britain the matter is regulated by a statutory provision to the effect that "subject to any agreement, express or implied, between the partners, . . . a partner making, for the purpose of the partnership, any actual payment or advance beyond the amount of capital which he has agreed to subscribe, is entitled to interest at the rate of five per cent per annum from the date of payment or advance."[2]

(*b*) *Firm Assets Insufficient to Repay Advances.* — If the assets of the partnership are insufficient for the repayment of advances, the creditor partner must bear his proportion of the loss,[3] unless he is exempted therefrom by agreement. In Magilton *v.* Stevenson,[4] it was agreed that the profits and losses should be borne equally by the four partners, "provided, however, that the said Magilton shall in no event be put to a loss of more than $1,250, and the balance shall be made up and paid to him, in case of greater loss, by the other parties." Magilton, having advanced all the funds used by the partnership to the amount of $4,770, and the business having proved a total failure, recovered a joint and several judgment against his copartners for $3,520. Interest thereon was allowed in his favor after his demand for the balance, on the ground that the defendants had unjustly refused to "adjust the accounts in accordance with the agreement."

[1] Folsom *v.* Marlette (Nev.), 49 Pac. 39 (1897); Burdick's Cases on Part. 570, and cases cited 572.

[2] British Partnership Act, § 24 (3). See Lindley on Part. (6th ed.) 391, for authorities prior to the Act.

[3] Nowell *v.* Nowell, L. R. 7 Eq. 538 (1869). One partner had advanced £1900, and the net assets were £1400. The deficiency had to be borne equally by the partners.

[4] 173 Pa. St. 560; 34 At. 235 (1896); Burdick's Cases on Part. 573.

### § 3. Repaying Capital.

We have seen that partners may stipulate that their contributions to the firm stock shall not be treated as capital owing from the firm to them, but shall be dealt with upon distribution as profits.[1] It is also possible for them to agree that money or property, furnished by one of them for the firm's use, shall not become the property of the firm, but that the title and the risk shall remain in the original owner.[2]

Such agreements are unusual, however. Ordinarily, the ownership of property contributed by the partners vests in the firm,[3] and the firm becomes indebted to them respectively for the capitals thus contributed. It follows, therefore, that in the absence of agreement to the contrary, "if the assets of the partnership, upon a final settlement, are insufficient to satisfy this" indebtedness, "all the partners must bear it in the same proportion as other debts of the partnership."[4] Nor does it matter that the capital is contributed wholly by one partner. To the extent of such contribution he is a creditor of the firm, and if the firm assets are insufficient to pay the debt to him, he is entitled to contribution from his copartners.

"If the matter be tested by one adventure," said Vice Chancellor James,[5] "the rule is made very clear. Two persons engage in a speculation, say in the purchase of £1,000 worth of cotton. One partner has the £1,000 at his command, the other has not. The first partner advances his £1,000 for the purpose of the speculation. If the cotton produces £1,100, the £100 is divided between the

[1] *Supra*, Chap. VIII. § 1 (A.).

[2] Heran *v.* Hall, 1 B. Mon. (Ky.) 159 (1840).

[3] Taft *v.* Schwamb, 80 Ill. 289 (1875); Burdick's Cases on Part. 577.

[4] Whitcomb *v.* Converse, 119 Mass. 38 (1875); Burdick's Cases on Part. 575.

[5] Nowell *v.* Nowell, L. R. 7 Eq. 538, 541 (1869).

two parties. If it only produces £900, could it be contended that the capitalist partner is to put up with the entire loss; and that the game of partnership between the man without money, and the man with, was to be on the principle of 'Heads, I win; tails, you lose'?"

(*a*) *Insolvency of one or more Partners.* — In case some of the partners are insolvent, the capital losses and deficiencies, like other partnership losses, must be borne by the solvent partners, in the proportion in which they were entitled to share profits. Thus, in Whitcomb *v.* Converse,[1] one of the four partners being insolvent, and they having agreed that each should receive one fourth of the profits, it was decreed in equity that the three solvent partners should contribute equally towards the loss of capital.

Moreover, when some of the partners are non-residents, and thus wholly beyond the reach of process, losses must be borne by the resident, solvent partners in the proportion stated above.[2]

(*b*) *Interest on Capital.* — Partnership articles often provide that the capitals contributed by the various partners, shall bear interest at a specified rate, especially if the contributions are unequal.[3] In the absence of an agreement, either express or implied, however, interest is not allowed on capital. Even though one partner furnishes all the capital, the courts will infer that the parties considered the skill and labor of the other as a contribution of equal value to the earning power of the firm.[4]

In case one partner has paid in his capital, and the other has not, the former should not be allowed interest on his

[1] 119 Mass. 38 (1875); Burdick's Cases on Part. 575.

[2] Henry *v.* Jackson, 37 Vt. 431, 438 (1865); Scott *v.* Bryan, 96 N. C. 289; 3 S. E. 235 (1887).

[3] Taft *v.* Schwamb, 80 Ill. 289 (1875); Burdick's Cases on Part. 577; Keiley *v.* Turner, 81 Md. 269; 31 At. 700 (1895).

[4] Jackson *v.* Johnson, 11 Hun (N. Y.), 509 (1877).

contribution in the absence of an agreement for interest. This is not a loan, and stands upon a different footing from an advance by a partner.[1]

An agreement for interest on capital does not extend beyond the dissolution of the firm, unless the parties have clearly evinced their intention to the contrary.[2] "The reason for this general rule is obvious. During the partnership, all the partners have the benefit of the capital to make profits, while upon dissolution this benefit ceases."[3]

### § 4. Adjusting the Equities of Partners.

Although the assets of a firm are to be applied in paying its debts to outsiders before either partner is to receive any part thereof, the individual creditors of a partner are not entitled to the same priority. They have a right to his individual interest only, and this, as has been stated repeatedly, is his "share of what may remain after payment of the partnership debts, and after a settlement of the accounts between the partners."[4]

1. The Lien of a Creditor Partner. — From the principles stated above, it follows, that "if one partner has become more indebted to the firm" than his copartner, his share "will stand incumbered by a lien, to make good such deficit to his copartner."[5]

[1] Lindley on Part. (6th ed.) 391; British Part. Act, 1890, § 24 (4); Clark *v.* Warden, 10 Neb. 87 (1880). Some cases appear to state a contrary doctrine, but the decisions are based on the ground that the moneys furnished, nominally as capital, were really loans. See cases analyzed in Clark *v.* Warden, *supra*, and Ligare *v.* Peacock, 109 Ill. 94, 102 (1884).

[2] Barfield *v.* Loughborough, L. R. 8 Ch. 1 (1872); Bradley *v.* Brigham, 137 Mass. 545 (1884).

[3] Johnson *v.* Hartshorne, 52 N. Y. 173, 177 (1873).

[4] Bank *v.* Carrollton Ry., 11 Wall. 624 (1870).

[5] Warren *v.* Taylor, 60 Ala. 218 (1877); Burdick's Cases on Part. 580.

This is well illustrated by the case cited in the last note. Warren filed a bill for a partnership accounting and settlement against his copartner Taylor and Mrs. Benagh, a mortgagee of Taylor's interest in the firm. Taylor had given a mortgage on his share to Warren also, to indemnify the latter against the use of the firm name on a bill of exchange which was issued for Taylor's personal benefit, and was not taken care of by Taylor, but was paid with firm assets. As Warren's mortgage was recorded four days after Mrs. Benagh's mortgage, it was subordinate to hers, and he was obliged to rest his claim to priority upon his equities as a partner. This claim was denied by the Chancellor, but fully sustained by the Appellate Court. It was declared that Mrs. Benagh could realize under her mortgage "what Taylor could claim if he were suing Warren, and no more. She purchased no other right. She cannot complain of this; for, purchasing a partner's interest in partnership effects, it was her duty to inquire of the other partner, how the account stood between them."

(a) *No Lien for Non-partnership Indebtedness.* — The foundation of a creditor partner's lien being the obligation of the firm to indemnify him in respect to payments made or liabilities incurred in the firm business, or for the preservation of its property,[1] it is apparent that the lien does not include all claims which may be held by one partner against another; but that it is limited to claims which are properly items in the partnership account. The following remark of Lord Hardwicke[2] is in point: "In all partnerships, when more money is advanced by one partner, or even lent for a partnership account and trade, the share must be considered as liable; for nothing must be divided as the share of the partner, but what is coming clear on

1 British Part. Act, 1890, §§ 24 (2), 39.

2 Doddington *v.* Hallet, 1 Ves. Sr. 497 (1750).

the balance of the account; for when the final account comes to be made up, everything which is the subject-matter thereof must be valued."[1]

Clearly, debts accruing to one partner from another outside the partnership business cannot be brought into the firm accounts by the creditor,[2] unless the partnership articles permit him to bring them in.[3] With respect to such debts, the creditor partner stands on the same footing with all other individual creditors. If the debtor partner has died or made an assignment, the survivor or the solvent partner, as the case may be, must pay over the debtor partner's share to the personal representative or assignee, and prove with other separate creditors against the estate.[4]

(*b*) *If the Debtor Partner is Insolvent.* — Courts of equity have modified this rule, to some extent, when the insolvency of the debtor partner has been shown. A recent case in Wisconsin[5] affords a good illustration. The plaintiff brought an action for a partnership accounting and settlement. His copartners, who appear to have been in possession of the firm assets, alleged in their answers that the plaintiff was insolvent, and set up by way of counter-claim various claims owned by them severally. An order overruling plaintiff's demurrer to the part of the answer setting up these counter-claims was affirmed by the Supreme Court. The decision was based not on the right of the defendants to bring these claims into the partnership accounting, nor on the ground that

[1] *Cf.* Pierce *v.* Tiernan, 10 Gill & J. (Md.) 253, 266 (1838); Mumford *v.* Nicoll, 20 John. (N. Y.) 611 (1822).

[2] Nichol *v.* Stewart, 36 Ark. 612, 625 (1880).

[3] Niblack *v.* Harrison, 81 Ind. 278 (1887).

[4] Moffat *v.* Thomson, 5 Rich. Eq. (S. C.) 155, 161 (1852).

[5] Pendleton *v.* Beyer, 94 Wis. 31; 68 N. W. 415 (1896); Burdick's Cases on Part. 584. *Cf.* Nichol *v.* Stewart, *supra.*

such claims could be counter-claimed or set off against the plaintiff's right of action, either at common law or under the State statute, but on the ground that the insolvency of the plaintiff gave a court of equity jurisdiction to compel a set off.

"If," said the court, "on the accounting and settlement of the partnership matters, anything shall be found due the plaintiff from the partnership, and it should be paid over to him, it would, apparently, be impossible for the defendants to obtain satisfaction of their claims against him. Actions at law upon these claims would be futile. So it seems that justice requires whatever sum may be found due to the plaintiff shall be applied to the payment of these claims to the defendants."

2. Interest Payable by a Partner. — If it is shown upon an accounting that any partner has used the assets of the firm for his individual benefit, or has neglected unreasonably to account to his copartners for firm property put into his hands for the purpose of winding up firm affairs, he will be charged with interest on the fair value thereof by way of damages for the wrongful detention of money due to his copartners.[1] The mere fact, however, that firm property is in one partner's hands for the purpose of winding up firm affairs, will not of itself render him liable for interest on its value, nor will delay in settling accounts, if this is chargeable as much to his copartners as to himself.[2]

3. Costs of an Accounting. — The costs of litigation, incident to a partnership accounting and distribution, are usually paid out of the partnership assets, as a necessary expense of winding up firm affairs.[3] If there is no fund in court for distribution, the costs will be divided between

1 Buckley v. Kelly, 70 Conn. 411; 39 At. 601 (1898).

2 Randolph v. Inman, 172 Ill. 575; 50 N. E. 104 (1898).

3 Gyger's Appeal, 62 Pa. 73 (1869); Burdick's Cases on Part. 586.

the parties, ordinarily.[1] But in case the court is of the opinion that one party necessitated the litigation, by putting an unauthorized construction on the partnership contract,[2] or by other misconduct, he will be charged personally with the payment of costs.[3]

When the assets of the firm are more than sufficient to pay its debts, including the claims of partners for advances and capital, the costs, when chargeable against firm effects, will be paid before profits are divided.[4] They will not be paid, however, in preference to the claims of a partner for advances[5] or for capital;[6] and if one partner is indebted to the firm, he must make good what is due from him to the assets, before he is entitled to have the costs paid out of the assets.[6]

### § 5. The Good Will of the Firm Business.

The legal rules upon this subject are not in a very satisfactory state. This is due, in part, to the fact that the "good will of a partnership" is one of the most modern topics in this modern branch of English law. Watson[7] does not allude to it. Montague's[8] comments upon it are confined to half a page. Gow[9] refers to but

[1] Groth *v.* Kersting, 23 Col. 213; 47 Pac. 393 (1896); Burdick's Cases on Part. 562; Folsom *v.* Marlette, 49 Pac. (Nev.) 39 (1897); Burdick's Cases on Part. 570; Austin *v.* Jackson, 11 Ch. D. 942 *n.* (1879).

[2] Taft *v.* Schwamb, 80 Ill. 289 (1875); Burdick's Cases on Part. 577.

[3] Hamer *v.* Giles, 11 Ch. D. 942 (1879).

[4] Mattingly *v.* Stone's Adm'r, 35 S. W. (Ky.) 921 (1896); Burdick's Cases on Part. 516, and cases in the next two notes.

[5] Potter *v.* Jackson, 13 Ch. D. 845 (1880).

[6] Ross *v.* White [1894], 3 Ch. 326; Burdick's Cases on Part. 587.

[7] Watson on Partnership (1st ed. 1794).

[8] Montague on Partnership (1st Am. ed. 1824), 211, citing only Farr *v.* Pearce, 3 Madd. 74 (1818).

[9] Gow on Partnership (2d Eng. ed. 1825), 377.

three cases bearing on the subject, from which he draws the conclusion that the good will of a professional partnership survives, but that it seems doubtful whether the good will of a trading firm survives, or forms a portion of the partnership stock. Chancellor Kent disposes of the topic in three sentences, the first of which is as follows: "The good will of a trade is not partnership stock."[1]

This doctrine, based upon a decision of Lord Loughborough,[2] has been rejected both in Britain and in this country, but neither the judiciary nor the legislature has substituted for it a complete and consistent body of principles.

1. What is "Good Will"? — The term has not received an authoritative definition in Britain. Lord Justice Lindley[3] has expressed the opinion that the term "can hardly be said to have any precise signification"; and Sir Frederick Pollock[4] has observed that it is "a commercial rather than a legal" term. "It is well understood in business," he adds, "but not easy to define."

In a few of our States it has received legislative definition. For example, the Civil Code of California declares: "The good will of a business is the expectation of continued public patronage, but it does not include a right to

[1] 3 Kent's Comm. *64.

[2] Hammond *v.* Douglas, 5 Ves. 539 (1800). Doubted by Lord Eldon in Crawshay *v.* Collins, 15 Ves. 227 (1808), but reaffirmed by Shadwell, V. C., in Lewis *v.* Langdon, 7 Sim. (1835). The non-survivorship of partnership good will was recognized by Lord Hardwicke in Gibblett *v.* Read, 9 Mod. 459 (1743).

[3] Lindley on Partnership (6th ed.), 441.

[4] Pollock's Digest of Partnership (6th ed.), 109. In his original draft of the Partnership Act, this learned author did not attempt to define the term, but contented himself with formulating the rules governing the rights of partners as to the good will, and the rights and duties of the vendor and the purchaser thereof. These rules formed Art. 57 of the 1st ed., and are reprinted with some modifications in the 6th ed. at pages 107 and 108.

use the name of any person from whom it was acquired. The good will of a business is property, transferable like any other."[1]

(*a*) *Judicial Definitions.* — One of the fullest and most important of these is that given by Vice-Chancellor Wood in Churton *v.* Douglas. Referring to Lord Eldon's statement[2] that "the good will which has been the subject of sale, is nothing more than the probability that the old customers will resort to the old place," he says:[3] "But it would be taking too narrow a view of what is there laid down by Lord Eldon to say that it is confined to that. 'Good will,' I apprehend, must mean every advantage, — every positive advantage, if I may so express it, — as contrasted with the negative advantage of the late partner not carrying on its business, whether connected with the premises in which the business was previously carried on, or with the name of the late firm, or with any other matter carrying with it the benefit of the business. When Lord Eldon is speaking of a nursery garden, or a locality which the customers must frequent to look at the plants and other things; and when Sir Thomas Plumer, in another case, is speaking of a retail shop which a person must enter in order to buy the goods there exposed — they are only, as it appears to me, giving those as illustrations of what good will is. But it would be absurd to say, that, where a large wholesale business is conducted, the public are mindful whether it is carried on at one end of the Strand or the other, or in Fleet Street, or in the Strand, or any place adjoining, and that they regard that, and do not regard the identity of the house of business, — namely, the firm. . . . When you are parting with the

[1] §§ 992, 993. These provisions have been enacted in Montana, Civil Code, §§ 1371, 1372, and in North Dakota, Civil Code, §§ 3486, 3487.

[2] Cruttard *v.* Lye, 17 Ves. 335, 346 (1810), and in other cases.

[3] Churton *v.* Douglass, H. R. V. Johns. 174, 188 (1859).

good will of the business, you mean to part with all that good disposition which customers entertain towards the house of business identified by the particular name or firm, and which may induce them to continue giving their custom to it. You cannot put it anything short of that."

This definition has been approved expressly in a recent decision of the House of Lords,[1] and has formed the basis of many judicial definitions in this country.[2]

2. PARTNERSHIP GOOD WILL IS PROPERTY. — Although the good will of a partnership is rarely, if ever, valued by a firm at its annual stock-taking and entered upon its books as an asset,[3] nevertheless it may be a thing of great value. "Often it happens," to quote from an eminent judge,[4] "that the good will is the very sap and life of the business, without which the business would yield little or no fruit. It is the whole advantage, whatever it may be, of the reputation and connection of the firm, which may have been built up by years of honest work, or gained by lavish expenditure of money." In such case, it may be taken into account in determining whether at a given date the partnership was solvent.[5]

(a) *May not be Valuable.* — While it is always a part of the firm property,[6] so long as the partnership is a going

[1] Trego *v.* Hunt [1896], App. Cas. 7, 17.

[2] Chittenden *v.* Whitbeck, 50 Mich. 401 (1883); Snyder Mfg. Co. *v.* Snyder, 54 Ohio St. 86; 43 N. E. 325 (1896); Menendez *v.* Holt, 128 U. S. 514, 522; 9 Sup. Ct. 143 (1888).

[3] Steuart *v.* Gladstone, 10 Ch. Div. 626, 659 (1879).

[4] Lord Macnaghton in Trego *v.* Hunt [1896], App. Cas. 7; Burdick's Cases on Part. 602, 604.

[5] Bell *v.* Ellis, 33 Cal. 620, 625 (1867).

[6] Statutes cited above, and Potter *v.* Commissioner, 10 Exch. 147 (1854), holding that the transfer of a partner's interest in the good will of the business is a conveyance of property and liable to *ad valorem* duty. It was valued by the parties at £20,000.

concern, in some partnerships it may have little or no money value.

Some judges have gone so far as to assert[1] that there is no salable good will in a professional partnership, because it "has no local existence, but is entirely personal, depending upon the trust and confidence which persons may repose in the integrity and ability" of its members. This view is based largely upon Lord Eldon's narrow definition of good will. The better doctrine appears to be that such partnerships have a good will which may or may not possess a money value, according to the circumstances of each case.[2]

This is in accord with English decisions relative to the good will of commission merchants and stock-brokers.

In Steuart *v.* Gladstone,[3] it was held that the plaintiff, who had been expelled from a firm, was not entitled to have the good will valued as an asset in taking the partnership account. This decision was not based on the ground that such a partnership was not possessed of a good will, but on the ground that the nature of the business and the language of the partnership articles disclosed an intention that the good will should not be included in the accounts to be taken upon dissolution. In Wilson *v.* Williams,[4] the Vice-Chancellor declared that the good will of a firm of stock-brokers would be valueless to any purchaser who did not also purchase the business premises or get the protection of a covenant preventing the retiring

[1] Austen *v.* Boys, 2 De G. & J. 626, 636 (1858); Hoyt *v.* Holby, 39 Conn. 326, 328 (1872).

[2] Lindley, L. J., in Arundell *v.* Bell, 52 L. J. Ch. 537, 540 (1883).

[3] 10 Ch. Div. 626 (1879).

[4] L. R. 29 Ir. Ch. 176, 181 (1892); *cf.* Warfield *v.* Booth, 33 Md. 63 (1870), sale of "his good will of practice" by a physician who agreed to "quit the practice in favor of" the purchaser; Dwight *v.* Hamilton, 113 Mass. 175 (1873), sale by a physician of "his practice and good will."

partners from carrying on the business within certain limits or from using the partnership name.

(*b*) *The Good Will may be Dissipated.* — Even when the good will is susceptible of a money valuation, it may be dissipated and lost by the acts of the partners. This will occur "when a firm is dissolved, its effects distributed, or sold in parcels to purchasers not wishing to embark in a similar business, and its affairs are wound up." Such acts render "the good will unavailable as a salable article, for it is not a distinctive article of property which may be sold separate from the tangible effects of the partnership."[1]

3. Good Will is to be Converted into Cash. — "On the dissolution of a partnership every partner has a right, in the absence of an agreement to the contrary, to have the good will of the business sold for the common benefit of all the partners."[2]

If they cannot agree upon the disposition to be made of the business, the court will appoint a receiver, upon a bill filed to close the partnership concerns, who will continue the business, if continuance be practicable, until it can be sold to best advantage as a going concern, and thus the full value of the establishment be realized by the partners.[3] If it is impossible for a receiver to conduct the business, he must sell immediately.[4] In the meantime every partner will be enjoined from conducting the same business, but not from conducting a similar business, if he carries it on as his own, and in such a manner as to indicate that it is not the business of the old firm.[5]

[1] The Snyder Mfg. Co. *v.* Snyder, 54 Ohio St. 86, 94; 43 N. E. 325 (1896); *cf.* Menendez *v.* Holt, 128 U. S. 514, 522 (1888).

[2] Pollock's Dig. of Part. (6th ed.) 107.

[3] Marten *v.* Van Schaick, 4 Paige's Ch. (N. Y.) 479 (1834).

[4] Williams *v.* Wilson, 4 Sand. Ch. (N. Y.) 380 (1846).

[5] Dayton *v.* Wilkes, 17 How. Pr. (N. Y.) 510 (1859). See the de-

(*a*) *Duty of a Surviving Partner.* — It would seem to follow from the principles stated above that the surviving partner is bound not only to sell the good will of the partnership business, but to bring it to a sale in the most advantageous manner and under such circumstances that it will produce the largest sum for all the parties interested.[1] Some courts have held him to a strict performance of this duty;[2] or have compelled him to account for the amount which the good will would have produced if it had been brought to such a sale.[3]

It must be admitted, however, that other courts have permitted the survivor to destroy the salability of the partnership good will by engaging at once in a new business of the same kind, at the same place, and in substantially the same name.[4] Undoubtedly, the survivor ought not to be precluded from carrying on the same line of business, after the firm affairs are wound up, in the absence of a contract on his part to withdraw from competition; and upon a sale of the good will, the purchaser ought to be advised that the survivor is at liberty to exercise this right;[5] but the survivor ought to be prevented from destroying or voluntarily impairing the salability of the good will.

crees in the last three cases, and also Seton's Forms of Decrees (5th ed.), 588 to 593 and 1799 to 1819.

[1] *Cf.* Mellersh *v.* Keen, 28 Beav. 453 (1860), not a case of surviving partner.

[2] Fenn *v.* Bolles, 7 Abb. Pr. (N. Y.) 202 (1858). The representative of the deceased partner obtained an injunction against the survivor's carrying on the firm business, and a receiver to sell the firm business and good will and wind up the affairs of the firm.

Rammelsberg *v.* Mitchell, 29 Ohio St. 22, 55 (1875).

[4] Loebeck *v.* Lee-Clark-Andreesen Co., 37 Neb. 158; 55 N. W. 650; 23 L. R. A. 795 (1893); Scudder *v.* Ames, 43 S. W. 659; 142 Mo. 187 (1897).

[5] Davis *v.* Hodgson, 25 Beav. 177, 182 (1858).

4. THE RIGHTS OF A PURCHASER. — In the absence of express stipulations to the contrary, the purchaser of all the partnership property, wherever situated, becomes the owner of the good will.[1] Moreover, the purchaser acquires the sole right to hold himself out as the successor to the business of the firm.[2] If the name of the old firm is a part of the good will, the purchaser would seem to acquire a right to use the name, to the exclusion of the sellers, "subject to this qualification, that the purchaser may use the vendor's name only 'so long and so far as he does not by so doing expose him to any liability.' The purchaser has the right to trade as the vendor's successor, but not to hold out the vendor as still in the business and personally answerable."[3]

Such is undoubtedly the established doctrine in England, and it has been approved by some of our courts.[4] Others, however, have declared that "the purchaser will not, in the absence of an express agreement, be allowed to continue the business in the name of the old firm."[5]

5. THE RIGHTS OF THE SELLER. — In the absence of express stipulations to the contrary, the sellers of a partnership good will may engage in the same line of business

[1] Hoxie *v.* Chaney, 143 Mass. 592; 10 N. E. 713 (1886); Jennings *v.* Jennings (1898), 1 Ch. 378.

[2] Pollock's Dig. of Part. (6th ed.) 108; Churton *v.* Douglass, H. R. V. Johns. 174, 190 (1859).

[3] Pollock's Dig. of Part. (6th ed.) 109, citing Levy *v.* Walker, 10 Ch. Div. 436 (1879); Thynne *v.* Shove, 45 Ch. Div. 577 (1890). *Cf.* In re Fraser, Ex parte Central Bank (1892), 2 Q. B. 633; Burdick's Cases on Part. 108, holding that a retired partner who consents that the continuing partner may use the old firm name, is not liable to the creditors of the new business as a partner by estoppel.

[4] Snyder Mfg. Co. *v.* Snyder, 54 Ohio St. 86; 43 N. E. 325 (1896).

[5] Williams *v.* Farrand, 88 Mich. 473 (1891); Burdick's Cases on Part. 588; Morgan *v.* Schuyler, 79 N. Y. 490 (1880). This is the rule of the California statute, *supra*, 351.

in the same locality and under their own names,[1] unless the use of such names amounts to a representation that they are the successors of the old firm.[2]

This doctrine was established at a time when contracts in restraint of trade were under popular and judicial disfavor. In the language of a distinguished judge: "Courts of equity could not of course enforce, even in a modified form, and within reasonable limits, an agreement, express or implied, which the law would have held void on the ground of public policy; nor could they treat the mere non-observance of such an agreement as fraudulent or inequitable. And so it has resulted that a person who sells the good will of his business is under no obligation to retire from the field."[3]

The seller, therefore, "may do much to regain his position, and yet keep on the windy side of the law. . . . He may do everything that a stranger to the business, in ordinary course, would be in a position to do."[3] Indeed, it was held in England at one time,[4] as it still is held in many of our jurisdictions,[5] that he may solicit the customers of the old firm.

Such is no longer the rule in England, the House of Lords having declared that "it is not an honest thing to pocket the prize and then to recapture the subject of sale, to decoy it away, or call it back before the purchaser has had time to attach it to himself and make it his very own."[3]

[1] Williams *v.* Farrand, 88 Mich. 473 (1891).

[2] Churton *v.* Douglass, H. R. V. Johns. 174 (1859).

[3] Lord Macnaghton in Trego *v.* Hunt [1896], App. Cas. 7, 24, 25; Burdick's Cases on Part. 602. Followed in Jennings *v.* Jennings [1898], 1 Ch. 378.

[4] Pearson *v.* Pearson, 27 Ch. Div. 145 (1884).

[5] Williams *v.* Farrand, *supra;* Cottrell *v.* Mfg. Co. 54 Conn. 138; 6 At. 791 (1886).

This doctrine does not apply to a sale in bankruptcy.[1] The purchaser of the good will of a bankrupt's business enters into no contract with the bankrupt, and has no legal right to complain if, after his discharge in bankruptcy, the former owner sets up in the same line of business and solicits old customers.

6. Partnership Stipulations Concerning the Good Will. — Attention has been called to the fact that the foregoing rules are subject to modification by agreements between the partners. The partnership articles often have provisions covering this topic, and they ought to have them always. Such provisions may relate to the manner of valuing the good will,[2] or may determine the time and circumstances of its sale, or may provide that it shall belong to the continuing or the surviving partner.[3] Agreements of this character simplify the questions connected with the good will of a firm, and make their solution an easier matter for the courts.

In the absence of stipulation upon the subject, if the value of the good will cannot be arrived at by a sale, it will be estimated at one or more year's purchase of the average net annual profits of the business.[4]

[1] Walker *v.* Mottram, 19 Ch. Div. 355 (1881).

[2] Wade *v.* Jenkins, 2 Giff. 509 (1860). The articles declared the good will should be valued at £6,000.

[3] Blake *v.* Barnes, 26 Abb. N. C. 208 (1890); Trego *v.* Hunt (1896), App. Cas. 7; Burdick's Cases on Part. 602.

[4] Mellersh *v.* Keen, 28 Beav. 453 (1860). The clerk to whom an inquiry was directed found that "the good will was worth one year's purchase of the net annual profits of the banking business, calculated on an average of the last three years," viz. £2,299 13*s.* 7*d.* This was affirmed by the Master of the Rolls.

# CHAPTER IX.

## LIMITED PARTNERSHIPS.

### § 1. Their Origin and Nature.

EACH member of a partnership is liable, according to English law, for all the partnership obligations. He may evade this liability by keeping his connection with the firm a secret; but he cannot exempt himself from it by any agreement with his copartners. In other words, the common law of England does not permit a partner to limit his liability for firm debts to his contribution to its capital, although he may have no voice in its management, and although he may stipulate in the partnership contract that his loss shall not extend beyond his contribution.[1]

1. THE CREATURES OF LEGISLATION. — Limited partnerships,[2] therefore, wherever the English common law prevails, are the creatures of statutes, which were suggested by certain provisions in the French Code of Commerce. New York was the pioneer[3] in this line of legislation, followed closely by Connecticut,[4] and then by

[1] Clift *v.* Barrow, 108 N. Y. 187 (1888); Burdick's Cases on Part. 93.

[2] Called special partnerships in some States. See Civ. Code of Cal. § 2477 *et seq.*

[3] Ch. 244, L. 1822. Chancellor Kent has remarked upon this as "the first instance in the history of the legislation of New York, that the statute law of any other country than that of Great Britain has been closely imitated and adopted." 3 Comm. 36. For some of the important differences in the two statutes, see Jacquin *v.* Blusson, 11 How. Pr. (N. Y.) 385 (1855).

[4] The Connecticut statute was adopted in 1822, a few months later than the New York Statute. See Clapp *v.* Lacey, 35 Conn. 463 (1868); Burdick's Cases on Part. 611.

other States and Territories; until, at present, legislative authority for limited partnerships exists in nearly every political jurisdiction of the United States.

The experiment has not commended itself to British legislators. An attempt was made to introduce a system of limited partnership, when the Law of Partnership was codified in Britain, but without success,[1] and the institution is still "unknown in the United Kingdom, and these kingdoms alone, or almost alone, among all the civilized countries of the world."[2]

(*a*) *Distinctive Characteristic of Limited Partnership.* — This consists in "the conjunction of at least one managing partner who is liable without limit for the partnership debts, like a partner in an ordinary firm, with one or more contributing partners who do not take an active part in the business, and are liable only to the extent of what they contribute to its capital."[2]

(*b*) *Limited Partnership Associations.* — The statutes of some jurisdictions[3] authorize a second form of limited partnership, "in which the capital subscribed shall alone be responsible for the debts of the association, except under certain circumstances." If the statutory provisions are complied with, none of the partners in these associations are subject to any personal liability. The business is conducted by a board of managers; the association sues and is sued in the association name; real estate is held, owned, and conveyed in the association name, and the

[1] Pollock's Dig. of Part. (3d ed.) Appendix.

[2] Pollock's Essays in Jurisprudence, 100.

[3] In Pennsylvania, Act of June 2, 1874, Brightly's Purd. Dig. (12th ed.) 1086–1088; in Virginia, Act of March 2, 1875, Code of 1877, §§ 2878–2886; in Michigan, Act of May 22, 1877, 1 Howell's Statutes, §§ 2365–2375; in New Jersey, Act of March 12, 1880, 2 Gen. Statutes, 2440; in Ohio, Act of April 20, 1881, R. S. (17th ed.) 773. Germany has adopted this form of Limited Partnership. See 9 Law Quar. Rev. 62, for comments on the statute passed April 20, 1892.

association is permitted to adopt and use a common seal. Such associations are very similar to the statutory joint stock companies of Britain and New York.

They have some of the characteristics of a corporation, but for most purposes they are treated by the courts not as corporate bodies, but as partnerships.[1] Some of the principal reasons assigned for this doctrine are these: "The formation of a limited partnership association is materially different from the creation of a corporation. Such association is treated in the statute as a partnership, which, upon the performance of certain acts, shall possess specified rights and immunities. In contemplation that the association may consist of many members, for convenience, it is clothed with many of the features and powers of a corporation, such as the right to sue and be sued, grant and receive, in the association name. But no man can purchase the interest of a member, and participate in the subsequent business, unless by a vote of a majority of the members in number and value of their interests. No charter is granted to the persons who record their statement."[2]

2. Limited Partnership is a True Partnership. — Although limited partnership is the creature of statutes, it is not a new species of legal institutions.[3] It is a common law partnership, but modified in certain respects by statutory provisions. It results from the voluntary contract of the parties, and is not a relation into which they are forced

[1] ~~Edwards v. Warren~~, 168 Mass. 564; 47 N. E. 502 (1897); Burdick's Cases on Part. 615.

[2] Eliot *v.* Himrod, 108 Pa. St. 569 (1885).

[3] The Louisiana civil code divides partnerships into commercial and ordinary partnerships, and subdivides the former into general and special, and the latter into universal and particular. It then declares that "partnership *in commendam*," or limited partnership, is "a modification of which the several kinds of partnerships are susceptible, rather than a separate division of partnerships."

by the law. "Both as to the rights of the parties to the contract, and as to the world, it is in itself a proper partnership, except as it limits the liability of the special partner, and restricts his control over the business of the firm. The members are partners, and by slight irregularities may easily be turned into general partners. The statute terms them partners; except for the statute they would be general partners, and from participating in the profits, it would seem to be a just consequence that they are partners in every sense, subject to liabilities and enjoying privileges as partners in every particular, except as otherwise specially provided. The common law regulates the mutual rights, and duties, and liabilities of partners, and governs these limited partnerships, in every respect not excepted out of the general rule by this statute."[1]

Accordingly, as held in the case last cited, the death of any partner, whether general or special, dissolves the firm, in the absence of a stipulation to the contrary between the partners. And undoubtedly a limited partnership is dissolved by operation of law whenever an ordinary partnership would be so dissolved.[2] Moreover, it may be dissolved, at any time, by the acts of the parties.[3]

(*a*) *Purpose of Limited Partnership Legislation.* — The principal object which legislators had in view, in authorizing limited partnerships, was the encouragement of trade. In the language of a leading case[4] on this subject:

[1] Ames *v.* Downing, 1 Brad. (N. Y. Surrogate's Court) 321 (1850); Burdick's Cases on Part. 606. This case contains a valuable historical sketch of Limited Partnership.

[2] Wilkins *v.* Davis, 2 Lowell (U. S. C. C.), 511; 15 N. B. R. 60 (1876); bankruptcy of a general partner. See Pepper & Lewis's Digest, Vol. 1, p. 2696, § 34, for Pennsylvania rule, in case of insolvency of special partner.

[3] *Cf.* L. of N. Y., 1897, Ch. 420, § 42. See § 13, *infra.*

[4] Clapp *v.* Lacy, 35 Conn. 463 (1868); Burdick's Cases on Part. 611, 613.

"Looking, then, to the statute as a whole, and its history, in connection with the then condition of commercial law, we find a clear, general purpose and intent of the legislature to encourage trade by authorizing and permitting a capitalist to put his money into partnership with general partners possessed of skill and business character only, without becoming a general partner, or hazarding anything in the business except the capital originally subscribed." The same view has been expressed by other courts.[1]

### § 2. Who may Compose Them.

In the absence of express statutory provisions on the subject, any person can become a member of a limited partnership who can become a member of an ordinary firm. Hence, the fact that one of the general partners in a limited partnership is a minor, does not affect the liability of the special partner. The contract of partnership between the minor and his copartners, is not void, but voidable only.[2] Even in the case of an ordinary partnership, as we saw in an earlier chapter,[3] the infant cannot withdraw from the firm his contribution, as against its creditors. Certainly he cannot make such a withdrawal from a limited partnership whose assets, in case of insolvency, are treated by the statutes as to some extent a trust fund for ratable distribution among its creditors.[4]

In a jurisdiction where married women are emancipated from common law disabilities, and are authorized to incur

[1] Singer *v.* Kelly, 44 Pa. 145, 149 (1863); Riper *v.* Poppenhausen, 43 N. Y. 68 (1870); Burdick's Cases on Part. 653, 655.

[2] The Cont. Nat. Bank *v.* Strauss, 137 N. Y. 148; 32 N. E. 1066 (1893); Burdick's Cases on Part. 619.

[3] *Supra*, Chap. III. § 1.

[4] See L. of N. Y. 1897, Ch. 420, § 40; Innes *v.* Lansing, 7 Paige (N. Y. Ch.), 583 (1839); Crouch *v.* First Nat. Bank, 156 Ill. 342; 40 N. E. 974 (1895); Burdick's Cases on Part. 667.

contract liabilities as if they were unmarried,[1] they may become members of limited partnerships.[2]

(*a*) *The Number of Partners.* — As a rule the statutes provide that two or more persons may form a limited partnership, one or more of whom shall be general partners, and the others shall be special partners.[3] Occasionally, two or more general partners [4] are required, and in some jurisdictions the number of special partners is limited.[5] The statutes, authorizing limited partnership associations, require three or more to unite in the organization.[6]

### § 3. Requisites to their Formation.

In addition to a contract between the parties, the statutes require them to do certain acts before a limited partnership shall be deemed to be formed. While there is considerable difference in matters of detail, the general provisions of the statutes on this topic are substantially the same.[7] The most important acts are those of making a specified certificate and affidavit, of registering and publishing these documents, and of making the advertised contribution of capital by the special partner.

1. Contents of the Certificate. — The certificate, which the partners severally are required to sign and acknowledge, must state (1) The name under which the

[1] Steffen *v.* Smith, 159 Pa. St. 207; 28 At. 295 (1893).

[2] Benard *v.* Packard, 64 Fed. 309; 12 C. C. A. 123 (1894); Burdick's Cases on Part. 623.

[3] L. of N. Y. 1897, Ch. 420, § 30. This statute requires all members to be of full age.

[4] Gen. St. of Wash. § 2917.

[5] Code of Md., Art. 73, § 2.

[6] Pa., Act of June 2, 1874, § 1. Ohio limits the number to twenty-five; R. S. § 3161 *a*.

[7] Since the New York statute has been the basis of similar legislation in most of the States, its provisions will be referred to more frequently than those of any other enactment.

partnership is to be conducted; (2) The general nature of the business intended to be transacted; (3) The names and residences of all the partners, specifying which are general and which are special partners; (4) The amount of capital contributed by the special partners; (5) The times at which the partnership is to begin and end.[1]

(*a*) *Rules of Statutory Construction.* — In some cases courts have shown a disposition to give a harsh and technical construction to limited partnership statutes, on the ground that they are in derogation of the common law.[2] Undoubtedly they were enacted for the protection of the special partner, and were intended to confer upon him a privilege which was denied by the common law; but, as already pointed out, they had another purpose in view, that of encouraging trade. Accordingly, they have been treated by most courts as remedial statutes, which are entitled to a liberal construction.

This view is well stated in the following extract from the prevailing opinion in a New York case: "In one aspect, of course, it (a limited partnership) is a privilege, because at common law no such partnership could be formed, but at the same time the granting thereof accords with the policy of a commercial community, because it tends to the enlargement of business transactions to permit men under certain reasonable conditions to do business with a restricted liability, who without such

[1] L. of N. Y. (1897) Ch. 420, § 30; Cal. Civ. Code, § 2479.

[2] In Jacquin *v.* Buisson, 11 How. Pr. (N. Y.) 385, 393 (1855), Hoffman, J., spoke of the English common law as "the strong enemy of limited partnerships;" and Judge Woodruff declared in another case that "parties cannot claim under the statute, which derogates from the general rule of law, without showing a strict compliance with the statute;" In re Merrill, 12 Blatch. 221, 224; Fed. Cas. No. 9467 (1874). Similar views are expressed in Pierce *v.* Bryant, 5 Allen (Mass.), 91 (1862); Burdick's Cases on Part. 631; and Durant *v.* Abendroth, 69 N. Y. 148 (1877).

restriction would suffer a portion of their capital to remain unemployed, rather than risk their whole possessions under the broad liability of a general partnership. Therefore acts providing for the formation of a limited partnership should receive a reasonable construction, not such as to make its formation almost impossible."[1]

Wherever this doctrine prevails, all that is requisite to the valid formation of a limited partnership is an honest and substantial compliance with those statutory provisions which are conditions precedent to its existence.

(*b*) *The Partnership Name.* — Not only must the names of the various members of the partnership be stated in the certificate, and the general partners be distinguished from the special partners, but the partnership name must be set forth. The rule upon this point, it will be observed, is radically different from that which obtains in the case of an ordinary partnership, where a name is not essential to the firm's existence.[2] That a firm name should be agreed upon, stated in the certificate, and published to the world, is not only a reasonable, but it is a necessary requirement in the cases of limited partnerships. Without it, the registration of these firms would be of little value, for their identity could not be established by mere inspection of the public records.

Generally the statutes permit the insertion of the names of general partners only in the firm name. Often they prohibit the use of a special partner's name in the firm style, under the penalty of his being liable as a general partner, if his name is so used with his privity.[3] The purpose of such provisions is "doubtless to prevent

[1] Manhattan Co. *v.* Laimbeer, 108 N. Y. 578, 582; 15 N. E. 712 (1888). See dissenting opinion for argument in favor of a narrow construction, at p. 600.

[2] *Supra*, Chap. III. § 1.

[3] L. of N. Y. (1897) Ch. 420, § 35.

credit being given to a person not liable as a general partner for the debts or liabilities of the firm."[1]

In some States, however, the name of a special partner may appear in the firm name, when the limited partnership succeeds to the business of a former firm, whose name it adopts in a manner authorized by statute.[2]

(c) *The Use of "and Company."* — The statutes are far from uniform upon this point. In some States, the names of all the general partners must appear in the firm name and the use of the words "and Company" or "and Co." is not allowed.[3] In other States, these words may be added to the names of one or more of the general partners, if there are more than one,[4] while in still others, there is no statutory provision on the subject.[5] Even when the use of these words is prohibited, their insertion in the firm name may not subject the special partner to the liabilities of a general partner. Whether it does or not depends upon the language of the statute. If their use is prohibited, but no penalty is attached to this violation, while the statute declares that certain other violations of its requirements shall subject the special partner to the liabilities of a general partner, their prohibited use neither prevents a limited partnership from being formed nor converts it into a general partnership.[6]

[1] Buck *v.* Alley, 145 N. Y. 488; 40 N. E. 236 (1895); Burdick's Cases on Part. 624.

[2] Groves *v.* Wilson, 168 Mass. 370; 47 N. E. 100 1897); Burdick's Cases on Part. 630; the New York statute appears to permit this, §§ 20, 21.

[3] Civil Code of Ala. (1896) § 3220.

[4] L. of N. Y. (1897) Ch. 420, § 35; the statutory provisions on this point have been altered several times in New York.

[5] Cal. Civ. Code, §§ 2477–2510.

[6] Buck *v.* Alley, 145 N. Y. 488; 40 N. E. 236 (1895); Burdick's Cases on Part. 625. See Andrews *v.* Schott, 10 Pa. St. 47 (1848), *contra.*

(*d*) *The Nature of the Business.* — While a certificate which describes the business of the partnership as that of "general dealers" does not satisfy the statute,[1] it is not necessary that it should set forth all the details of the partnership agreement,[2] nor that its statement of the nature of the business should be in the very words of the partnership articles.[3] In the case last cited the court held the certificate to be valid, although it described the firm's business as "a general commission business, buying and selling grain, flour, and produce on commission," while the articles declared that the partnership was formed "for the purpose of carrying on a general produce and commission business."

That the certificate should disclose the nature of the firm business, clearly and honestly, follows both from the affirmative requirement of the statutes and from the fact that limited partnerships are prohibited from engaging in particular kinds of business, notably banking and insurance.[4] Certainly the certificate ought to show whether or not the partnership is engaged in a prohibited business; for if it is so engaged, the special partner is not entitled to the privileges accorded by the statute to such a member of the firm, but is subject to all the liabilities of a general partner.[5]

(*e*) *The Amount of Capital Contributed.* — It is of the highest importance to those dealing with the firm that the certificate should contain a definite and trustworthy statement of the amount of capital contributed by the special partner. Hence, in almost every case, the statute requires

[1] Benedict *v.* Van Allen, 17 Up. Can. Q. B. 234 (1859).

[2] Metropolitan Nat. Bank *v.* Sirrett, 97 N. Y. 320; 15 Abb. N. C. 318 (1884); Burdick's Cases on Part. 633.

[3] Manhattan Co. *v.* Phillips, 109 N. Y. 383; 17 N. E. 129 (1888).

[4] See L. of N. Y. (1897) Ch. 420, § 30.

[5] McGehee *v.* Powell, 8 Al. 827, 835 (1846).

an affidavit by one or more of the general partners, or by all the partners, that the sums specified in the certificate to have been contributed by the special partners have been actually and in good faith paid in cash; and it declares that if any false statement be made in the certificate or affidavit all the persons interested in the partnership shall be liable for all its engagements as general partners.

Substantial compliance with these provisions is necessary, unquestionably, to the formation of a limited partnership; and in many States this is expressly asserted in the statutes.[1] The following language from a decision of the New York Court of Appeals[2] expresses the unanimous opinion of the courts upon this subject: "The amount contributed by the special partner is an essential part of the terms of the partnership. The mode of contribution is just as explicitly fixed as that there shall be a contribution; and it is just as explicitly required that the mode of contribution prescribed by the statute shall be followed, and shall be averred in the affidavit, as that there shall be an amount of contribution, and that the amount shall be stated. To guard against unsafe practices and to secure the public against even innocent deception, or mistake, the statute demands that a limited partner shall pay into the capital a sum which he shall specify; that he shall make 'actual cash payment' of that sum. . . . The purpose was that a limited partnership should start in its business on a fixed and certain basis, with a sum in its possession of that which does command the markets, and makes the possessor of it equal, as a buyer, to any other, and to its extent as solvent as any other."

(*f*) *Contributed Cash may be Invested in Goods at Once.* — In Van Ingen *v.* Whitman, cited in the last note,

[1] Cal. Civ. Code, § 2482; N. Y. L. 1897, Ch. 420, §§ 33, 34.

[2] Van Ingen *v.* Whitman, 62 N. Y. 513, 519 (1875). See Pierce *v.* Bryant, 5 Allen (Mass.), 91 (1862); Burdick's Cases on Part. 631.

the special partner did not make a cash contribution to the capital of the limited partnership, but being entitled to an interest in the assets of a former firm to an amount of more than $30,000, he authorized one of the general partners to convert it into cash, and to pay the cash into the new firm. There was no evidence that this ever was done, although it did appear that the limited partnership acquired the special partner's interest in the former firm's assets, the estimated value of which was not disputed. It was held that a limited partnership had not been formed. The affidavit and accompanying papers made out a presumptive case, it was said, that the partnership was a limited one; but this case was overthrown by evidence of the affidavit's falsity.

The court did not hold, however, that had the special partner paid the $30,000 in cash to the general partners, they could not have used their capital thus acquired in buying the assets of the former firm; and in a later case the Court of Appeals has held [1] that such a purchase is valid. The special partner, said the court, did not receive the purchase price "as a return of his capital paid in. The transaction on his part was not in form or in legal effect the same as though he had put in the goods as part of his capital, instead of the money. The money when paid was beyond his control, and placed in the legal possession of the general partners, and was subject to any disposition they might make of it. The purchase, in effect, was a transaction of the firm after the firm had been organized, and not the consummation of a prior contract, or at least the jury were at liberty so to find."

Later in its opinion the court said: "If the purchase of the stock was made a condition of his contribution of capital, a different question would be presented." That very

[1] Metropolitan Nat. Bank *v.* Sirrett, 97 N. Y. 320 (1884); Burdick's Cases on Part. 633.

question was presented in a subsequent case, and the same court declared[1] that when such a condition attends the contribution of capital by the special partner, his payment cannot be upheld as one made in good faith, for the new firm has "only the sight of money, but no continued possession nor any benefit of it." The appropriation is made before the firm's formation.

(*g*) *Contribution of Property other than Cash.* — In a few States the special partner is not required to make his contribution to firm capital in cash, but may put in other forms of property. Here, again, the statutory requirements must be carefully complied with. He must describe the property so that creditors may ascertain from the certificate and affidavit the real character of the firm assets, and may estimate intelligently the credit to which the partnership is entitled.[2] If the statute provides that the property shall be valued by all the partners, such a valuation must be made, and an honest statement of the facts must be incorporated in the certificate.[3]

The courts do not construe these statutes, however, as imposing impossibilities upon persons, nor permit them to operate as traps "to catch those who have honestly complied with their substantial requisites." If the property is described with sufficient fulness "to enable parties dealing with the partnership to ascertain readily the kind, amount, and value of the contribution to its capital," and if the other provisions of the statute have been complied with substantially and honestly, the validity of the limited partnership will be sustained.[4]

[1] Manhattan Co. *v.* Phillips, 109 N. Y. 383; 17 N. E. 129 (1888); Lineweaver *v.* Slagle, 64 Md. 465; 2 At. 693 (1886), *accord.*

[2] Holliday *v.* Union Bag Co., 3 Col. 342 (1877).

[3] First Nat. Bank of Danville *v.* Creveling, 177 Pa. St. 267; 35 At. 595 (1896); Burdick's Cases on Part. 638.

[4] Robbins *v.* Weber, 172 Pa. St. 635; 34 At. 116 (1896).

(*h*) *When must the Contribution be made?* — Although there is some authority for the proposition that the special partner must make his statutory contribution before the affidavit and certificate are executed,[1] the better view appears to be that he complies with the statute if he makes his contribution before those papers are filed. "It is the act of filing the certificate and affidavit which gives life to the partnership and confers immunity from the debts of the firm upon the special partner, and from that moment those who deal with the partnership become entitled to know the truth as to its formation, and from and after that time a wrong is done to those who deal with it, if a false statement is published through the filing of the certificate. The truth of the statements contained in the certificate is to be determined, therefore, at the time of its being filed with the county clerk. If true at the instant of filing, there is no liability, because, being true at the instant of the creation of the limited partnership, they fulfil the purpose for which the law was enacted."[2]

If, however, the special partner does not make the contribution until a week after the filing of the papers and the commencement of business by the firm, his liability for all partnership engagements is that of a general partner.[3] It will not matter that the intentions of the parties were honest, nor that firm creditors cannot show that they have been harmed by this non-compliance with a plain and peremptory requirement of the statute. The acts have not

[1] Durant *v.* Abendroth, 69 N. Y. 148 (1877).

[2] Ropes *v.* Colgate, 17 Abb. N. C. 136, 143 (1886), cited and approved in White *v.* Eiseman, 134 N. Y. 101 (1892); Burdick's Cases on Part. 640.

[3] Myers *v.* Edison General Electric Co., 59 N. J. L. 153; 35 At. 1070 (1896); Burdick's Cases on Part. 644.

been done which alone entitle the special partner to exemption from firm engagements.[1]

If there are two or more special partners, the failure of either to comply with the essential requirements of the statute, although the others have done all the acts required of them, will be fatal to all. Each special partner is compelled to see that every other member of the firm complies with the statute.[2]

(*i*) *A Check as Cash.* — There is practical unanimity on the part of the courts in holding that a special partner does not contribute cash to the firm, when he turns over to it promissory notes,[3] or stocks or bonds.[4] Nor is a post-dated check to be considered as cash.[5] But "where the money is actually in the bank to the credit of the special partner, and he gives absolute and final control of it to the general partner" by delivering to him a certified check, or a check which the general partner procures to be certified, the transaction has been held to amount to a payment of cash.[6]

2. Registration of Certificate and Affidavit. — In order to secure a permanent public record of every limited partnership, the statutes require the certificate and affidavit to be filed, and the certificate to be recorded, in a designated office, usually the clerk's office of the county where the principal place of business of the partnership is located and if it has places of business in different

[1] Pierce *v.* Bryant, 5 Allen (Mass.), 91 (1862); Burdick's Cases on Part. 631.

[2] Whittemore *v.* Macdonell, 6 Up. Can. C. P. 547 (1857).

[3] Pierce *v.* Bryant, *supra*. Promissory notes of the special partner, who was a man of large wealth.

[4] Haggerty *v.* Foster, 103 Mass. 17 (1869). United States bonds payable to bearer and worth more than par.

[5] Durant *v.* Abendroth, 69 N. Y. 148 (1877).

[6] White *v.* Eiseman, 134 N. Y. 101; 31 N. E. 276; Burdick's Cases on Part. 640.

counties, a certified copy of the certificate must be filed and recorded in the clerk's office of each county.[1]

Until this requirement is complied with, the partnership is not formed as a limited partnership.[2] It is made the duty of the partners to deliver the documents at the proper office for filing and recording, and to leave them there. If they receive them back and retain them, negligently supposing the law to have been complied with, the business carried on will be that of a general partnership.[3] The law does not impose upon them, however, the duty of supervising the county clerk, or of compelling him to perform his duty. "When the parties have done all that they can do in the way of complying with the terms and conditions of the limited partnership act, and when all that remains to be done is for a public officer (entrusted with the care and custody of the papers filed with him) to perform the duties placed upon him under the provisions of the law, it must be regarded as a compliance by the parties interested with the terms of the statute, and the record must be assumed to be made when the paper goes for the purpose of record out of the control of the individual into the control of the public officer."[4]

3. Publication of the Certificate. — The statutes usually impose upon the partners the duty of promptly publishing, in the local or other newspapers, either the certificate or the terms of the partnership for a designated period, and of filing proof of the publication with the original certificate;[5] although some statutes authorize a

[1] L. of N. Y. (1897) Ch. 420, §§ 30, 31; Cal. Civ. Code, § 2480; La. Civ. Code, § 2848.

[2] L. of N. Y. (1897) Ch. 420, § 33; Cal. Civ. Code, § 2482.

[3] Henkel *v.* Heyman, 91 Ill. 96 (1878).

[4] Manhattan Co. *v.* Laimbeer, 108 N. Y. 578; 15 N. E. 712 (1888).

[5] The Cal. Civil Code, § 2483, calls for the publication of the certificate. So does the present New York statute; L. 1897, Ch. 420, § 32. The Revised Statutes called for the publication of the terms of the

publication by posting notices, "if there be no newspaper published in the county."[1] When publication is required, it generally is declared to be a condition precedent to the legal existence of a limited partnership. Not only are the partners bound to see that the publication is made, but they are bound to see that all the material facts are accurately stated in the published announcement. If the special partner's contribution is mistakenly stated in one of the newspapers, to be $5,000, when it is but $2,000, the error will prove fatal.[2] The misspelling of a name,[3] or the duplication of it,[4] or a mistake in the date when the partnership is to begin business,[5] will be treated generally as immaterial errors.

When the statute provides that the publication shall be made "immediately after" the filing of the certificate, the requirement is satisfied if the publication begins within a week or ten days after the filing.[6] Nor will the publication be deemed invalid, because one of the designated newspapers changes its name during the statutory period of publication.[7]

### § 4. Notice to Creditors.

The registration of the statutory certificate by a limited partnership, not only gives to those dealing with it an opportunity to learn the nature of its business, but it

partnership, Part II. Ch. IV. Tit. I. § 9. The original New York act did not require a publication.

1 Maryland Code, Art. 73, § 7.

2 Smith *v.* Argall, 6 Hill (N. Y.), 479 (1844); s. c. on appeal, 3 Den. (N. Y.) 435 (1846).

3 Bowen *v.* Argall, 24 Wend. 496 (1840).

4 Carter-Battle Grocer Co. *v.* Jackson, 45 S. W. 615 (Tex. Civ. App.) (1898).

5 Madison Co. Bank *v.* Gould, 5 Hill (N. Y.), 309 (1843).

6 Manhattan Co. *v.* Phillips, 109 N. Y. 383; 17 N. E. 129 (1888).

7 Metropolitan Bank *v.* Sirrett, 97 N. Y. 320 (1884); Burdick's Cases on Part. 633, 638.

operates as constructive notice to them upon this subject. Accordingly, if the certificate describes the business as that of "the purchase, sale, and manufacture of all kinds and descriptions of furniture," every one dealing with the general partners is bound to know, that a contract for the purchase of clothing for the individual general partners to be paid for with furniture belonging to the firm, is not within the usual course of business of the firm, and, therefore, that they have no implied authority to bind the firm by such a contract.[1]

Nor have the general partners the power to change the business of the firm, without the special partner's consent. Their practices, therefore, which are inconsistent with the nature and scope of the business, as set forth in the certificate, do not warrant third persons in assuming that the scope of the business has been changed.[2]

### § 5. Creditors may be Estopped.

Undoubtedly a special partner who has not complied with the substantial requirements of the statute, may exempt himself from the liability of a general partner by an express stipulation made with those who contract with the firm.[3] But has he the right to say that persons who have become creditors of the firm, knowing that it claims to be a limited partnership, are estopped from insisting that it is a general partnership, and that he is liable as a general partner? The principles which are found to obtain in the case of joint stock companies,[4] as well as the

[1] Taylor *v.* Rasch, 11 N. B. R. 9; 1 Flip. 385 (1875); Burdick's Cases on Part. 646.

[2] Singer *v.* Kelly, 44 Pa. St. 145 (1863); Burdick's Cases on Part. 674.

[3] See opinion of Gibson, J., in Hess *v.* Werts, 4 S. & R. (Pa.) 356, 361 (1818).

[4] *Supra*, 27 *et seq.*

plain declaration of the statutes,[1] would seem to lead to a negative answer; and this answer has been given by some courts.[2]

In other jurisdictions, however, it has been held that persons who become creditors of a limited partnership, with knowledge of its defective organization, are estopped from denying its valid existence;[3] and the Supreme Court of Michigan has gone so far as to hold that a creditor of a limited partnership association, having dealt with and trusted the association, as a body of persons with a limited liability, cannot recover against its members either as individuals or as general partners.[4]

(*a*) *An Advising Creditor.* — A person who has advised and assisted in the defective organization of a limited partnership ought not to be allowed to allege thereafter that the partnership was not lawfully launched, and that the special partner was liable to him as a general partner.[5]

[1] Cal. Civil Code, § 2482; L. of N. Y. (1897), Ch. 420, § 33. In substance, that no limited partnership is formed until the statutory requirements are complied with.

[2] Manhattan Brass Co. *v.* Allin, 35 Ill. App. 336 (1889); Sheble *v.* Strong, 128 Pa. St. 315; 18 At. 397 (1889). In the latter case it is said: "The question is not one of good faith on the part of the defendants, or of notice to creditors, but whether, in their attempt to form a limited partnership, they conformed to the law. If they did not, their attempt was abortive, and it is no defence that creditors had actual knowledge of the facts required to be set out in the recorded statement."

[3] Tracy *v.* Tuffly, 134 U. S. 206; 10 Sup. Ct. 527 (1889); Burdick's Cases on Part. 647.

[4] Staver Mfg. Co. *v.* Blake, 111 Mich. 282; 69 N. W. 508 (1896); Burdick's Cases on Part. 649. The court declared that the rule should be applied in this case which is applied in the case of a defectively organized corporation. See *upra*, Chap. I. § 4.

[5] Allegany Nat. Bank *v.* Bailey, 147 Pa. St. 111; 23 At. 439 (1892).

(*b*) *Estoppel by Judgment.* — If a creditor brings an action against all the members of a limited partnership, as general partners, and judgment is rendered in favor of the special partner against the creditor, but in favor of the creditor against those named in the certificate as general partners, that judgment is a bar to any other action by the same creditor proceeding upon the theory that the special partner has made himself liable as a general partner, for it conclusively determines that he was not a general partner.[1]

An adjudication in bankruptcy against a limited partnership, upon the petition of a general partner, does not estop its creditors from denying that it was legally organized under the statute, and from asserting that the special partner is liable as a general partner. In the bankruptcy proceeding, no issue is raised between the creditors and special partner as to the validity of the partnership organization, nor are the creditors parties to the proceeding. Consequently the adjudication is wholly *ex parte*, so far as the creditors are concerned, and cannot operate as an estoppel upon them. They remain at liberty, even after taking dividends in the bankruptcy proceedings, to show that the pretended limited partnership was not organized in conformity with the statute, and that the special partner's liability to them was unlimited.[2]

(*c*) *Defective Organization does not Invalidate Firm*

[1] Bell *v.* Merrifield, 109 N. Y. 202; 16 N. E. 55 (1888). The judgment was held not a bar, however, to an action against the special partner for an unlawful withdrawal of capital.

[2] Durant *v.* Abendroth, 97 N. Y. 132 (1884). In Sheble *v.* Strong, 128 Pa. St. 315, 18 At. 397 (1889), it was held that a judgment against a limited partnership association did not estop the judgment creditor from maintaining a subsequent action against its members as general partners. Under the Pennsylvania statute, the two actions are different in form and effect; the parties are not the same, and the issues involved are different.

*Contracts.* — A limited partnership is not an illegal association, simply because the statutory requirements have not been complied with upon its organization. Non-compliance with the statute enables a creditor to hold all the members of the firm as general partners, but it does not relieve a firm debtor from his liability to the partnership, nor does it invalidate contracts made with the firm.[1]

### § 6. Removal to Another County.

The statutes provide for the registration of limited partnerships in a public office [2] of the locality in which the firm has its principal place of business, and the publication of the certificate in local newspapers.[3] These provisions are intended to secure to the local business public "full knowledge of the situation of the firm." As a rule, however, the statutes do not authorize the removal of a limited partnership from one county, or similar subdivision of a State, to another, nor do they provide in any way for such a change in its place of business. Accordingly, it has been held that if a limited partnership, although properly organized under the statute, discontinues its business in the original county and removes to another, the special partners will no longer enjoy the protection of the statute, but will become liable as general partners in the business carried on in the new location.[4]

[1] Clement *v.* British Am. Assurance Co., 141 Mass. 298; 5 N. E. 847 (1886); Briar Hill Co. *v.* Atlas Works Co., 146 Pa. St. 290; 23 At. 326 (1892).

[2] In California, the office of the recorder of the county, Civ. Code, § 2480. In Louisiana, the office for mortgage records, Rev. Civ. Code, Art. 2848. In New York, the county clerk's office, L. 1897, Ch. 420, § 32. In Alabama, the county probate judge's office, Civil Code of 1896, § 3212.

[3] *Supra*, Chap. IX. § 3.

[4] Riper *v.* Poppenhausen, 43 N. Y. 68 (1870); Burdick's Cases on Part. 653.

### § 7. Renewal Certificates.

The statutory provisions on this topic are quite indefinite, as will appear from the following section of the New York statute which has been copied with but few modifications in most of the States: "Every renewal or continuance of such partnership beyond the time originally fixed for its duration shall be certified, acknowledged, and recorded, and an affidavit of a general partner be made and filed, and notice given in the manner herein required for its original formation."[1]

It is not strange that courts have differed in their interpretation of this provision. In Pennsylvania, they have held that it requires a true statement not only of the capital originally contributed by the special partner, but of the fact that such capital is unimpaired at the time of renewal.[2] While in other jurisdictions they have declared that the renewal certificate and affidavit need not refer to the then condition of the special capital; that they are to be read in connection with the original papers; and that it is not a condition precedent to a valid renewal of the partnership, that its capital is unimpaired.[3]

### § 8. Ante-Partnership Negotiations.

These are to be distinguished from contract engagements entered into by a limited partnership before the statutory requirements have been complied with. In a recent Pennsylvania case, it appeared that negotiations were opened with the plaintiffs by certain members of a

[1] R. S. Pt. II. Ch. 4, Tit. 1, § 11. It has been shortened by L. of 1897, Ch. 420, § 33.

[2] Fourth Street Nat. Bank *v.* Whitaker, 170 Pa. St. 297; 33 At. 100 (1895); Burdick's Cases on Part. 655.

[3] Hogan *v.* Hadzets, 71 N. W. (Mich.) 1092 (1897); Burdick's Cases on Part. 660; Fifth Ave. Nat. Bank *v.* Colgate, 120 N. Y. 381; 24 N. E. 799 (1890); Arnold *v.* Danziger, 30 Fed. 898 (1887).

limited partnership before its certificate was filed or recorded, but that they did not ripen into a contract until after the partnership had complied with the statute. The court held, without hesitation, that the special partners were not liable as general partners upon the contract.[1] It is the status of the partnership when the contract is made, not when negotiations are opened, that determines the liability of the special partners.

Even when business has been carried on by a limited partnership before its certificate is filed and recorded, a subsequent compliance with the requirements of the statute entitles the special partner to its protection as to all business engagements entered into thereafter.[2]

### § 9. Partnership Capital.

The capital of a limited partnership, like that of a general partnership, is owned by the firm. A special partner, as we have seen, cannot make an actual contribution to firm capital, without parting with all his individual title to it. Any string attached to it for his benefit will render the organization of a limited partnership invalid. His contribution will be deemed illusory and not real.[3]

As soon as his contribution is made, "actually and in good faith," although it constitutes the entire capital of the firm, his individual title to it is gone. Thereafter the title is in the firm; and goods bought with it are firm goods. Accordingly, in a jurisdiction where the separate creditor of a general partner may levy an execution upon firm property, such a creditor may levy upon the goods of a limited partnership; and the special partner cannot maintain tres-

[1] Hinds *v.* Battin, 163 Pa. St. 487; 30 At. 164 (1894); Burdick's Cases on Part. 664.

[2] Levy *v.* Lock, 47 How. Pr. (N. Y.) 394; 5 Daly, 46 (1874).

[3] Manhattan Co. *v.* Phillips, 109 N. Y. 383; 17 N. E. 129 (1888); Lineweaver *v.* Slagle, 64 Md. 465; 2 At. 693 (1886).

pass against a sheriff for seizing the goods under such a levy, even though his contribution constituted the entire capital of the partnership.[1]

1. Withdrawal of Capital by Special Partner. — This is expressly prohibited by all of the statutes, although they are not agreed in their penalties for violations of the provision. In most States[2] it is declared that if the original capital has been reduced by the payment of interest or profits to any special partner, he shall restore the amount necessary to make good his share of capital with interest. In others, it is enacted that a special partner who withdraws capital from the firm, contrary to the statutory prohibition, thereby becomes a general partner.[3]

(*a*) *Bona fide Receipt of Interest or Dividends.* — The special partner is permitted to receive interest[4] on his capital or a proportion of the profits, if such payments do not reduce the original amount of his capital; and some statutes declare that he is not bound to refund such payments to meet subsequent losses.[5] If, however, the payments were made and received under the honest but mistaken belief that they did not reduce the special part-

[1] Bradbury *v.* Smith, 21 Me. 117 (1842); Burdick's Cases on Part. 666; Vandike *v.* Rosskam, 67 Pa. St. 330 (1871).

[2] N. Y. R. S. Part II. Ch. IV. Tit. I. §§ 15, 16. In § 39 of Ch. 420, N. Y. L. (1897), it is declared that such a special partner "becomes liable as a general partner for debts contracted until he returns such amount, to the extent of the amount so withdrawn."

[3] Cal. Civil Code, § 2495.

[4] Even when the statute refers to the *annual* receipt of interest, a provision in the partnership agreement that the special partner shall receive interest *monthly* does not violate the statute. Metropolitan Bank *v.* Sirrett, 97 N. Y. 320 (1884); Burdick's Cases on Part. 633, 637.

[5] Cal. Civil Code, § 2494. See dictum in Lachaise *v.* Marks, 4 E. D. Smith (N. Y.), 610, 625-626 (1855), to the same effect.

ner's capital, he is bound, upon discovering the mistake, to repay so much thereof as is necessary to make good his original capital.

(*b*) *Indirect Withdrawals.*—In Lachaise *v.* Marks, cited in the last note, Judge Woodruff remarked, that if the receipt of dividends by the special partner "was a device, resorted to in bad faith for the purpose of withdrawing his capital," it would render him liable as a general partner upon all firm engagements, thereafter entered into. The California statute declares that "no special partner, under any pretence, may withdraw any part of his capital invested by him in the partnership, during its continuance."[1]

In accordance with this doctrine it has been held that a special partner who sells his interest in the firm to his general partner and takes a chattel mortgage on the stock to secure the purchase price, before the partnership has been dissolved in the manner prescribed in the statute, violates the provision as to the withdrawal of capital.[2] This provision is also violated when the general partners assume as a firm obligation, a debt owing by the special partner for the money contributed by him to the partnership capital;[3] or when the general partners repay to the special partner his capital, at the expiration of the partnership, the firm then being insolvent.[4]

Such withdrawals of capital are also alterations in the

[1] Cal. Civil Code, § 2493.

[2] Beers *v.* Reynolds, 11 N. Y. 97 (1854). In Lachaise *v.* Marks, 4 E. D. Smith (N. Y.), 610 (1855), it was held that a contract for the sale of a special partner's interest, the transfer to take effect after the statutory dissolution, did not operate as a withdrawal of his capital at the time of making the contract, although the special partner received at that time the purchaser's negotiable promissory notes for the price, payable after the dissolution; distinguishing Beers *v.* Reynolds, *supra.*

[3] Coffin's Appeal, 106 Pa. St. 280 (1884).

[4] Baily *v.* Hornthal, 154 N. Y. 648; 49 N. E. 56 (1898).

capital and operate under another section[1] of the statute to make the special partner liable as a general partner.

(c) *Actions to Compel Restoration.* — The general partners, who have assented to the prohibited withdrawal of capital, cannot bring an action to compel the special partner to refund.[2] If, however, the latter has bound himself in the partnership articles to bear a certain share of the losses, the general partners can enforce this agreement by proper proceedings.[3] But the general partners' assent to the withdrawal cannot affect the rights of firm creditors. Still, if they seek to hold the special partner liable to the extent of his prohibited withdrawals, they are bound to show that they have already had recourse to the general partners to collect their claims and have exhausted their remedy at law against them in an unsuccessful effort to obtain payment thereof.[2] It has been intimated[3] that an assignee in bankruptcy of the general partner may maintain an action at law for the recovery of such withdrawals.

### § 10. Preferences Forbidden.

Following a provision of the earliest New York act,[4] the statutes generally declare that all transfers of property by a limited partnership or its members, as well as all judgments confessed, liens created, or securities given with the intent of giving a preference to any firm or individual creditor, over other creditors of the firm, are void as against the partnership creditors, if such acts are done by

[1] N. Y. R. S. Pt. II. Ch. IV. Tit. I. § 12; L. of 1897, Ch. 420, § 41.

[2] Bell *v.* Merrifield, 109 N. Y. 202, 209–210; 16 N. E. 55 (1888).

[3] Wilkins *v.* Davis, 2 Lowell, 511; Fed. Cas. No. 17,664; 15 N. B. R. 60, 67 (1876); Baily *v.* Hornthal, 154 N. Y. 648; 49 N. E. 56 (1898).

[4] L. of 1822, Ch. 242, § 9; now L. of 1897, Ch. 420, § 40. See the provisions of the Illinois statute in Burdick's Cases on Part. 669.

an insolvent partnership or partner, or in contemplation of insolvency.

(*a*) *The Meaning of Insolvency.* — To bring a preferential transfer or lien under the ban of this section, it is not necessary to show an adjudication in insolvency or bankruptcy, or that proceedings leading to such an adjudication were contemplated. On the other hand, it is not enough to show the commission of an act, by the firm or by a partner, which might subject him or the firm to an involuntary proceeding under an insolvency or bankruptcy statute. The term insolvency, in this connection, has been held to mean the financial condition of a firm or a partner whose property is insufficient to pay his debts.[1]

(*b*) *The Object of this Provision.* — We have seen in an earlier chapter,[2] that a general partnership or any of its members can make a valid transfer of firm or individual property to one firm creditor with the avowed intent to prefer him over all others. Such a right is denied to limited partnerships and their members. Clearly the Legislature intended to secure a *pro rata* distribution of the property of these partnerships, when insolvent, among all their creditors, if proper proceedings were instituted by them. It was held, therefore, in an early case[3] and has remained unquestioned,[4] that a creditor of an insolvent partnership is not bound to proceed to judgment and execution at law before filing a bill to set aside prohibited transfers, or to prevent future preferences; but that he may file a bill in behalf of himself and other creditors of the firm, and may have a receiver appointed to

[1] McArthur *v.* Chase, 13 Grat. (Va.) 683 (1857); Walkenshaw *v.* Perzel, 32 How. Pr. (N. Y.) 233; 4 Robt. 426 (1866).

[2] Chap. III. § 3.

[3] Innes *v.* Lansing, 7 Paige (N. Y. Ch.), 585 (1839).

[4] Crouch *v.* First Nat. Bank of Chicago, 156 Ill. 342; 40 N. E. 974 (1895); Burdick's Cases on Part. 667.

take the property and distribute it ratably among all the creditors who may come in and prove their debts under the decree.[1]

The statute does not prevent a vigilant creditor, however, from obtaining an advantage over other creditors in any manner. It does not invalidate every payment made or judgment suffered by an insolvent limited partnership. In the language of a leading case on this point, the statutory provisions "declare void only judgments confessed or liens created, — referring clearly to preferences expressly and voluntarily given by the partners, or one of them, fraudulently or in collusion with the creditor. They do not inhibit or apply to judgments recovered against the members of a limited partnership *in invitum*, or suffered by them by default or otherwise. They merely render void judgments confessed. The members of a limited partnership, before or after insolvency, are just as liable to be sued for their debts as other natural persons. Their creditors are entitled to recover judgments against them, with the view to reach the individual property as well as the partnership property. . . . The assets of a limited partnership are trust funds . . . when the courts of equity are properly appealed to in behalf of the partners, or any partner or creditor, to protect and distribute the same upon equitable principles, and on such application assert the control over them. . . . There is no rule in equity which makes them trust funds in any other sense, or which gives the court of equity any control over them, or which forbids any creditor of the copartnership or of any individual partner from ob-

[1] Kerr *v.* Blodgett, 48 N. Y. 62 (1871). In this case, after the partnership made a general assignment, which was executed by the general partner, a firm creditor brought an action on behalf of all creditors for an accounting and distribution by the assignee; and the court held that it was not the duty of the assignee to produce and prove the claims of firm creditors; and that only those who had proved their claims under the decree could share in the proceeds.

taining a lien on them by due process of law in any hostile proceedings." [1]

### § 11. Transformed into General Partnerships.

Although a limited partnership has been organized in strict conformity with the statute, it may be transformed into a general partnership, as regards creditors, without a new agreement between its members. Such a transformation is produced by certain violations of the statute, which we will now consider.

1. PROHIBITED INTERFERENCE BY A SPECIAL PARTNER. — As a rule, only the general partners are allowed to transact the business of a limited partnership. Legal proceedings are to be brought by them and against them, as though there were no special partners. In most jurisdictions they are bound to permit the special partners to "examine into the state and progress of the partnership business and advise as to its management;" [2] and some statutes permit them on behalf of the firm to borrow money or hire property from the special partners, and even to employ the latter as agents for specified purposes.[3]

If a special partner, however, interferes in the business affairs of the firm beyond the limits set by the statutes, they declare "he shall be deemed and be liable as a general partner." This stringent provision is rigorously enforced by the courts. A single clear violation of it by the special partner forfeits forever his statutory exemption from personal liability. It is an unpardonable offence. He cannot regain in that partnership his original status.[4]

[1] Van Alstyne *v.* Cook, 25 N. Y. 489, 493, 495 (1862); Hall *v.* Glessner, 100 Mo. 155; 13 S. W. 349 (1889).

[2] L. of N. Y. 1897, Ch. 420, § 37; Cal. Civ. Code, § 2490.

[3] Ohio Rev. Statutes of 1892, § 3153.

[4] Hutchinson *v.* Bowes, 15 Upper Can. Q. B. 156 (1858). The court said: "We think there is nothing in the point of his having ceased to interfere in the business before these goods were furnished."

Indeed such a violation makes him liable as a general partner in that partnership from the beginning.[1]

A special partner does not incur the statutory penalty by instituting an action for dissolution and becoming the receiver of the firm, where the firm's affairs have become embarrassed through the general partner's misconduct. Such an action is in the interest of creditors, and not a prohibited interference in the business affairs of the firm.[2]

2. Prohibited Alteration by a Special Partner. — Other acts by the special partner, which operate to transform the limited partnership into a general one, are those altering the names of the general partners, or the nature of the business, or the capital of the firm. It is of the utmost importance to those dealing with a limited partnership that none of the matters set forth in its registered certificate should be changed. Hence the severity of the penalty imposed upon the special partner who participates[3] in any such changes.

These alterations, when made with the assent of the special partner, are declared by the statutes, generally, to dissolve the firm, and if it is thereafter continued, to constitute it a general partnership as to all business thereafter transacted.[4] They have no retroactive effect, however,

[1] The First Nat. Bank of Canandaigua *v.* Whitney, 4 Lans. (N.Y.) 34 (1871); Farnsworth *v.* Boardman, 131 Mass. 115 (1881); *cf.* McKnight *v.* Ratcliff, 44 Pa. St. 156, 166 (1863), holding that a special partner, who had violated the statutory prohibition as to interference, was not liable as a general partner for a trespass by the other partners and their agents.

[2] The Continental Nat. Bank *v.* Strauss, 137 N. Y. 148 (1893); Burdick's Cases on Part. 619.

[3] In Singer *v.* Kelly, 44 Pa. St. 145 (1863); Burdick's Cases on Part. 674, it was held that the special partner should not suffer for attempted alterations by the general partners of which he was ignorant, and for which he was in no way responsible.

[4] L. of N. Y. 1897, Ch. 420, § 41; Cal. Civil Code, § 2507.

differing in this respect from prohibited acts of interference. Accordingly, it has been held that a suit brought by a limited partnership for the recovery of debts which accrued before a prohibited alteration, must be brought in the names of the original general partners, although when the suit was begun the partnership is a general partnership.[1]

In some States the special partner is permitted to increase his contribution to the capital stock, or to sell his share, and one or more special partners may be added to the partnership without working a dissolution or alteration, upon filing with the original papers an additional certificate or notice.[2]

### § 12. Creditors of the General Partners.

While the statutes commit the conduct of partnership affairs almost exclusively to the general partners, they do not treat these members as the individual owners of the firm property. Frequently they declare in express terms that the general partners "shall be liable to account to each other and to the special partners, for their management of the business, as other partners are at law."[3] Hence actions for the dissolution of a limited partnership and an accounting may be brought either by the general or the special partners,[4] and the rules of distribution and of

[1] Perth Amboy Manufacturing Co. *v.* Condit, 21 N. J. L. 659 (1847); Burdick's Cases on Part. 673. Actions upon claims accruing after the transformation of a limited into a general partnership, are properly brought in the names of all the partners. Sarmiento *v.* The Catherine C., 110 Mich. 120; 67 N. W. 1085 (1896); Burdick's Cases on Part. 678.

[2] L. of N. Y. 1897, Ch. 420, § 41. Upon this point, as upon many others relating to limited partnerships, the statutory provisions in each jurisdiction must be carefully consulted.

[3] Ibid. § 37.

[4] The Continental Nat. Bank *v.* Strauss, 137 N. Y. 148 (1893); Burdick's Cases on Part. 619. *Infra*, § 13 (3).

marshalling assets are those[1] which we have found to obtain in winding up the affairs of a general partnership.[2]

1. THE RIGHTS OF A MORTGAGEE OF A GENERAL PARTNER'S INTEREST. — Even when there is but one general partner, the mortgagee of his interest does not acquire a lien upon the firm property as against firm creditors. The lien extends only to the mortgagor's share in that property, which may be something or nothing of value. The mortgagee's "only recourse is on the residuum which might accrue to his debtor after the full liquidation of the partnership."[3]

2. ASSIGNMENT FOR CREDITORS BY THE GENERAL PARTNERS. — An assignment of firm property by the general partners in trust for creditors is void if it contains preferences.[4] If, on the other hand, it provides for a *pro rata* distribution of firm assets among the firm creditors, it is valid, although the special partner does not join in its execution.[5] This seems to follow from the broad powers of management conferred by the statutes on the general partners, and the strict prohibition upon interference by the special partner.

Whether the assent of a special partner to an assignment for creditors is necessary, when the statute has not been complied with or has been violated, so that he is liable to creditors as a general partner, is a question upon which the courts have differed. In New York, it has been held[6] that his assent is unnecessary; while in

[1] Van Alstyne *v.* Cook, 25 N. Y. 489, 493–495 (1862).

[2] *Supra,* Chap. V. VIII.

[3] Sherwood *v.* His Creditors, 42 La. Ann. 103; 7 So. 79 (1890); Burdick's Cases on Part. 678.

[4] L. of N. Y. (1897) Ch. 420, § 40.

[5] Schwartz *v.* Soutter, 103 N. Y. 683 (1886).

[6] Robinson *v.* McIntosh, 3 E. D. Smith, 221 (1854). In Durant *v.* Abendroth, 97 N. Y. 132 (1884), it is declared that a limited partnership remains such in form even though the special partner has so

Minnesota, not only his assent to the general partner's act, but an assignment of all his separate property, has been held necessary to the validity of the partnership assignment.[1] The latter holding is based upon the policy of the State insolvent law, which requires the surrender of all the property of each of the debtors who are parties to the assignment.

3. THE SPECIAL PARTNER AS A CREDITOR. — The contribution of the special partner to the firm capital does not entitle him to share in the firm estate with outside creditors. So far as his share of capital is concerned, he has no greater rights against the firm estate than any other partner has. Nor, in case he takes a mortgage on the general partner's interest in the firm, will his rights be different from those of any other individual creditor of such general partner.[2]

But, suppose he becomes a creditor of the firm by lending it money, or indorsing its paper, or selling property to it, what are his rights? In the absence of any statutory provision on the subject, he would be treated, probably, as an ordinary creditor. He could sue the firm and levy upon its property; or in case of insolvency, or bankruptcy, he could prove his claims and take ratable dividends thereon. As a rule, however, the statutes contain a provision that, in case of the insolvency or bankruptcy of a limited partnership, the special partner shall not be allowed to claim as a creditor until the claims of all the other creditors of the partnership are satisfied.

The courts have disagreed in their construction of this

acted as to enable creditors to treat him as a general partner, and if voluntary proceedings in bankruptcy are to be instituted, only general partners are to join in the petition.

1 In re Allen, 41 Minn. 430; 43 N. W. 382 (1889).

2 Sherwood v. His Creditors, 42 La. Ann. 103 (1890); Burdick's Cases on Part. 678.

clause. On the one hand, it has been limited to the special partner's claim for capital; and he has been permitted to prove and share ratably with other firm creditors, for loans made to the firm after its due organization.[1] On the other hand, the clause has been construed to extend to every claim acquired by the special partner against the firm during its existence; and the weight of authority is in favor of this view.[2]

The provision, however, does not apply to debts due from the limited partnership to a firm of which the special partner is a member,[3] nor to debts acquired by the special partner from *bona-fide* partnership creditors after the dissolution of the partnership.[4]

### § 13. Dissolution of Limited Partnerships.

In most respects, the rules relating to the dissolution of general partnerships are applicable to limited partnerships. The death of any member dissolves the firm as to all the partners.[5] It is dissolved, also, by the bankruptcy of a partner;[6] and by the expiration of the period for which it was organized, as stated in the certificate.

[1] Clapp *v.* Lacey, 35 Conn. 463 (1868); Burdick's Cases on Part. 611.

[2] White *v.* Hackett, 20 N. Y. 179 (1859); Dunning's Appeal, 44 Pa. St. 150 (1863); Jaffa *v.* Krum, 88 Mo. 669 (1886). In 1857 the New York statute was amended so as to permit the special partner to claim as a creditor in certain cases. See § 37 of Ch. 420, L. of N. Y. 1897, to the same effect.

[3] McArthur *v.* Chase, 13 Gratt. (Va.) 683, 697 (1857).

[4] Hayes *v.* Heyer, 35 N. Y. 326 (1866).

[5] Ames *v.* Browning, 1 Brad. (N. Y. Surrogates Court), 321 (1850); Burdick's Cases on Part. 606. The doctrine of this case is now qualified by § 41, Ch. 420, Laws of 1897, which permits the partnership to continue after the death of a partner, if the original articles provide for such a continuance.

[6] Wilkins *v.* Davis, 2 Low. 511; 15 N. B. R. 60; Fed. Cases, No. 17,664 (1876).

1. Dissolution by Expiration of Term. — As "the times at which the partnership is to begin and end" must be stated in the certificate, which is publicly registered, neither former dealers nor the general public are entitled to any notice of dissolution. They are bound to take notice of the terms of the certificate, as they are of the death or of the bankruptcy of a partner. Accordingly, if the general partners pretend to continue the business of the limited partnership, after its certified term, debts contracted by them in such business cannot be enforced, either against the former special partner,[1] nor against the assets of the limited partnership to the detriment of its creditors.[2]

2. Dissolution by Alteration. — Reference has been made in a former section to the statutory provision on this subject. Every alteration made in the names of the general partners, or in any matter which is an essential part of the original certificate, works a dissolution of the firm; and if the partnership be continued thereafter, it is continued as a general partnership.

3. Dissolution by Judicial Decree. — In a few jurisdictions, the statutes expressly provide that a limited partnership is subject to dissolution in the same manner as a general partnership;[3] but such a provision is not necessary to give a court of equity power to decree a dissolution for any cause which would warrant such a decree in the case of a general partnership. Accordingly, a dissolution may be ordered by the court where the special partner has been induced by fraud to enter the firm,[4] or where, through mistake, the organization is defective and the special

[1] Marshall *v.* Lambeth, 7 Rob. (La.) 471 (1844).
[2] Haggerty *v.* Taylor, 10 Paige, 261 (1843).
[3] Cal. Civ. Code, § 2509.
[4] Tournade *v.* Methfessel, 3 Hun (N. Y.), 144 (1874).

partner is liable as a general partner; [1] or where a general partner is guilty of serious mismanagement.[2]

4. Dissolution by Act of the Partners. — The statutes permit the partners to dissolve the partnership prior to the expiration of the certified term, but it is provided generally that this kind of dissolution shall not take effect until a notice thereof has been filed in the office where the original certificate is recorded, and until this notice has been published for a stated period in a designated manner.[3] Even though a dissolution has been agreed to by all the partners, and a notice thereof has been filed in the proper office, the partnership continues to be a limited partnership until the statutory publication has been completed. Hence, during this period it cannot give preferences; [4] and any prohibited interference by the special partner renders him liable as a general partner.[5]

[1] Patterson *v.* Holland, 7 Grant's Ch. (Up. Can.) 1 (1858).

[2] The Continental Nat. Bank *v.* Strauss, 137 N. Y. 148 (1893); Burdick's Cases on Part. 619, 622.

[3] L. of N. Y. 1897, Ch. 420, § 42; Cal. Civ. Code, § 2509.

[4] Fanshawe *v.* Lane, 16 Abb. Pr. (N. Y.) 71, 73 (1862).

[5] Buckley *v.* Bramhall, 24 How. Pr. (N. Y.) 455, 462 (1863)

# APPENDIX.

## THE PARTNERSHIP LAW OF NEW YORK.

(CHAPTER 420 OF THE LAWS OF 1897: CHAPTER LI. OF THE GENERAL LAWS.)

### ARTICLE I.

GENERAL PROVISIONS.

§ 1. **Short Title.** — This chapter shall be known as the partnership law.

§ 2. **Partnership Defined.** — A partnership, as between the members thereof, is the association, not incorporated, of two or more persons who have agreed to combine their labor, property and skill, or some of them, for the purpose of engaging in any lawful trade or business, and sharing the profits and losses, as such, between them.

§ 3. **General Partnership.** — A partnership formed otherwise than in the manner prescribed in this chapter for the formation of a limited partnership, is a general partnership.

§ 4. **Limited Partnership.** — A limited partnership consists of one or more persons, called general partners, and also one or more persons called special partners.

§ 5. **Authority of General Partner.** — Every general partner is agent for the partnership in the transaction of its business, and has authority to do whatever is necessary to carry on such business in the ordinary manner.

§ 6. **Liability of General Partner.** — Every general partner is liable to third persons for all the obligations of the partnership, jointly and severally, with his general copartners.

§ 7. **Liability of Special Partner.** — A special partner, except as declared in this chapter, is liable for the obligations of the limited partnership only to the amount of the capital invested by him therein.

## ARTICLE II.

### BUSINESS AND PARTNERSHIP NAMES.

§ **20. When Partnership or Business Name may be Continued.** — The use of a partnership or a business name may be continued, in either of the following cases.

1. Where the business of any firm or partnership in this State, having business relations with foreign countries or which has transacted business in this State not less than three years, continues to be conducted by some or any of the partners, their assignees, or appointees;

2. Where a majority of the members, general or special, of a general or limited partnership formed under the laws of this State, or of the stockholders of any corporation, domestic or foreign, which may theretofore have carried on its business within this State, and where said general or limited partnership or corporation has discontinued, or shall be about to discontinue its business within the State, and where a majority of the partners, general or special, in either of such last mentioned copartnerships or of the survivors thereof shall be members of the new limited copartnership, or where a majority of the members of such copartnership theretofore existing, or of the surviving members thereof or of the stockholders of such corporation shall consent in writing to the use of such firm or corporate name by the new limited partnership; or

3. Where any resident of this State dies, who at the time of his death and for at least five years immediately prior thereto, conducted and carried on in his sole name, any business in this State, or who at the time of his death, so conducted and carried on any business having relation with other States or foreign countries, the right to use the name of such person, for the purpose of continuing and carrying on such business, shall survive and pass and be disposed of and accounted for as part of the personal estate of such deceased person, and such business may be continued and carried on under such name by any person who comes into legal possession thereof.

§ **21. Certificate to be Filed and Recorded; Clerk's Fees.** — Whenever a partnership or business name continues

to be used as provided by the last preceding section, the person or persons using such name shall sign and acknowledge a certificate, declaring the person or persons intending to deal under such name, with their respective places of residence, and file the same in the clerk's office of the county where the principal place of business is located, and cause a copy of such certificate to be published once in each week for four consecutive weeks in a newspaper of the city or town in which such principal place of business is located, or if none be published in such city or town, in the newspaper nearest thereto. A county clerk with whom any such certificate is filed, shall keep a book in which all such certificates shall be recorded, with their date of record, and also a register in which shall be entered in alphabetical order the name of every such partnership and of the partners thereof, and every such business name of a deceased person and the names of persons filing certificates therefor. The clerk is entitled to a fee of one dollar for filing and recording such certificate and entering such names, and to an additional fee of ten cents for every name of a partner beyond two, and to a fee of fifty cents for a certified copy of such certificate.

## ARTICLE III.

### LIMITED PARTNERSHIP.

§ 30. **Formation.**—Two or more persons may form a limited partnership, which shall consist of one or more partners of full age, called general partners, and also of one or more partners of full age, who contribute in actual cash payments, a specified sum as capital, to the common stock, called special partners, for the transaction within this State of any lawful business, except banking and insurance, by making, severally signing and acknowledging, and causing to be filed and recorded in the clerk's office of the county where the principal place of business of such partnership is located, a certificate, in which is stated:

1. The name or firm under which such partnership is to be conducted, and the county wherein the principal place of business is to be located;

2. The general nature of the business intended to be transacted;

3. The names, and whether of full age, of all the general and special partners interested therein, distinguishing which are general and which are special partners, and their respective places of residence;

4. The amount of capital which each special partner has contributed to the common stock;

5. The times at which the partnership is to begin and end.

If the partnership has places of business situated in different counties, a copy of the certificate, and of the acknowledgment thereof, certified by the clerk in whose office it is filed, under his official seal, shall be filed and recorded in like manner, in the office of the clerk of each such county.

§ 31. **Affidavit to be Filed.** — At the time of filing such original certificate, an affidavit of one or more of the general partners, stating that the sums specified in the certificate to have been contributed to the common stock by each of the special partners have been actually and in good faith paid in cash, shall also be filed in the same office, and a copy thereof certified by the county clerk, filed in each office in which a copy of the original certificate is filed.

§ 32. **Terms of Partnership to be Published.** — Immediately after the filing of the certificate, a copy of the same or a notice containing the substance thereof, shall be published once in each week for six successive weeks, in two newspapers of the county, in which such original certificate is filed, to be designated by the county clerk, one of which newspapers shall be a newspaper published in the city or town in which the principal place of business is intended to be located, if a newspaper be published therein; or, if no newspaper is published therein, in the newspaper nearest thereto, and proof of such publication by affidavit of the printer or publisher of each of such newspapers must be filed with the original certificate.

§ 33. **Renewal or Continuance of Partnership.** — Every such partnership may be renewed or continued beyond the time fixed for its duration, in the manner required for its original formation; and no such partnership shall be deemed to have been originally formed, or so renewed or continued, until a cer-

tificate is made, acknowledged, filed and recorded, an affidavit filed, and certificate or notice published as required by law.

§ 34. **Effect of False Statements or Failure to Publish Terms.** — If any false statement be made in any such certificate or affidavit, made either upon the formation or renewal or continuance or increase of capital of such partnership, or if any such certificate or notice is not so published, or if such partnership be renewed or continued in any other manner, the persons interested therein shall all be liable as general partners.

§ 35. **The Firm Name; List of Members to be Posted.** — The business of the partnership must be conducted under a firm name, which must consist of the name of the general partner, or if there be two or more general partners, of the names of one or more of such partners, with or without the addition of the words "and Company," or "and Co." If the name of any special partner be used in such firm name, with his privity, he shall be deemed and be liable as a general partner. The partnership must cause to be placed in a conspicuous place on the outside and in front of the building in which is its principal place of business, a sign on which is printed in legible English, the names in full, of all the members of such partnership, designating which are general and which are special partners. If such sign be not so placed, no action against the partnership shall abate or be dismissed by reason of the failure of the plaintiff to correctly allege in his pleadings, or prove as alleged the number and names of the members of the partnership; but his pleadings may be amended on the trial to conform to the proof in that respect, without costs.

§ 36. **Liability of Partners.** — The general partners in such partnership shall be jointly and severally liable as general partners are by law. The special partners shall not be liable for the debts of the partnership beyond the fund contributed by them respectively to the capital of the partnership.

§ 37. **General Powers of Partners.** — Except as provided in this section, the general partners only may transact the business of the partnership, and they shall be liable to account to each other and to the special partners, for their management of the business, as other partners are by law. Except as provided in this section, a special partner may not sign for the partner-

ship nor bind the same, nor transact any business on account of the partnership, nor be employed for that purpose, as agent, attorney or otherwise. A special partner may, from time to time, examine into the state and progress of the partnership business, and advise as to its management; may loan money to, and advance and pay money for the partnership; and may take and hold the notes, drafts, acceptances, and bonds of or belonging to the partnership, as security for the repayment of such money and interest, and may use and lend his name and credit as security for the partnership, in any business thereof, and has the same rights and remedies in these respects as other creditors might have; may lease to the general partner or partners any real or other property for the purposes of the partnership, at such rents and on such terms as may be agreed on; and may negotiate sales, purchases and other business for the partnership, but no business so negotiated is binding on the partnership until approved by a general partner. If a special partner interfere contrary to these provisions, he shall be deemed and be liable as a general partner. If such partnership become insolvent or bankrupt, a special partner shall not, except for claims contracted in pursuance of this section, be allowed to claim as creditor, until the claims of all the other creditors of the partnership are satisfied.

§ 38. **Actions by and against the Partnership.** — Actions and special proceedings in relation to the business of the partnership may be brought and conducted by and against the general partners, in the same manner as if there were no special partners.

§ 39. **Capital of Special Partner not to be Withdrawn; when he may Receive Interest.** — No part of the sum which any special partner contributes to the capital stock, shall be withdrawn by him or paid or transferred to him in the shape of dividends, profits or otherwise, at any time during the continuance of the partnership; but any such partner may annually receive lawful interest on the sum so contributed by him, if the payment of such interest does not reduce the original amount of such capital; and if, after the payment of such interest, any profits remain to be divided, he may also receive his portion of such profit. But, if by the payment of such interest or profits

to any special partner, the original capital is reduced, the partner receiving the same must restore the amount necessary to make good his share of capital, with interest, and he becomes liable as a general partner for debts contracted until he returns such amount, to the extent of the amount so withdrawn.

§ 40. **Fraudulent Transfers of Property by Partnership or Partner.** — Every sale, assignment or transfer of any of the property or effects of such limited partnership made by such partnership when insolvent or in contemplation of insolvency, or after or in contemplation of the insolvency of any partner, or of any of the property or effects of a general or special partner, made by any general or special partner, when insolvent or after or in contemplation of the insolvency of such partnership or such partner, with the intent of giving a preference to any creditor of such partnership, or insolvent partner over other creditors of the partnership, and every judgment confessed, lien created, or security given, by such partnership or partner, under the like circumstances, and with like intent, is void as against the creditors of the partnership.

Every special partner who violates this section, or concurs in, or assents to, any such violation by the partnership, or by any individual partner, is liable as a general partner.

§ 41. **Dissolution by Alteration; by Death of Partner; when Partnership may be Continued by Survivors.** — Except as provided in this section, every alteration made in the names of the general partners, in the nature of the business, or in the capital, or shares thereof contributed, held or owned, or to be contributed, held or owned, by any of the special partners, and the death of any partner, whether general or special, dissolves the limited partnership, or if such partnership be continued, constitutes such partnership, a general partnership, in respect to all business transacted after such alteration or death, unless the articles of partnership provide that, in the event of the death of a partner, the partnership may be continued by the survivors, in which case it shall be so continued with the consent of the personal representatives of the deceased partner, and personal representatives may succeed to the partnership rights of such deceased partner, and continue the business the same as if such partner had remained alive. But

any special partner may from time to time increase the amount of capital stock contributed, held or owned by him, or one or more special partners may be added to the partnership, on actually paying in an additional amount of the capital to be agreed on by the general and special partners, and on filing in the office of the clerk with whom the original certificate was filed, an additional certificate of the general partners in the partnership name, verified by the oath of one of them, stating the increase of such capital stock, and by whom, and the names and residences of such additional special partners, and whether of full age, and the amounts contributed by each to the common stock, together with the affidavit of one or more of the general partners stating that the sums specified in such additional certificate, have been actually and in good faith paid in cash; and such alteration does not make the partnership general. No additional publication of the terms of the partnership nor of the alteration thereof is required in any of the cases provided for in this section. Any special partner or the legal representatives of any such special partner, deceased, may sell his interest in the partnership, without working a dissolution thereof, or rendering the partnership general, if a notice of such sale be filed within ten days thereafter in the office of the clerk with whom the original certificate of partnership was filed, and the purchaser thereof thereupon becomes a special partner with the same right as an original special partner.

§ 42. **Dissolution by Act of Partners.** — A limited partnership may be dissolved by the acts of the partners before the time specified for its termination in the certificate of formation, renewal or continuance. But such a dissolution does not take effect until a notice of the dissolution has been filed with the clerk of the county in which the original certificate is filed and published at least once in each of four successive weeks in a newspaper published in each county where the partnership has a place of business.

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